IMPACT OF HIGH INTEREST RATES ON SMALL BUSINESS CAPITAL FORMATION

HEARING

BEFORE THE

SUBCOMMITTEE ON TAX, ACCESS TO EQUITY CAPITAL AND BUSINESS OPPORTUNITIES

OF THE

COMMITTEE ON SMALL BUSINESS HOUSE OF REPRESENTATIVES

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CONTENTS

Page

Hearing held on October 15, 1981 1

Nowak, Hon. Henry J., chairman, Subcommittee on Tax, Access to Equity Capital and Business Opportunities: Opening statement 1

Testimony of:
- Beck, Carl A., Charles Beck Machine Corp., on behalf of National Small Business Association; accompanied by Herbert Spira, tax counsel 88
- Carlson, Jack, executive vice president and chief economist, National Association of Realtors 2
- Doyle, Wilbur S., president, Doyle Lumber, Inc 70
- McGeady, M. Eamonn, president, Martin G. Imbach, Inc.; accompanied by Ronald Utt, associate chief economist, Chamber of Commerce of the United States, and David E. Franasiak, director, Tax Policy Center 99
- Napolitano, Frederick J., president-elect, National Association of Home Builders; accompanied by Robert D Bannister, senior staff vice president for Government affairs, and Jim Schuyler, staff vice president and legislative counsel for Government affairs 34
- Stoner, Robert, president, Winfield Industries; accompanied by Joe Cobb, director of economic analysis, Council for a Competitive Economy 41
- Zayas, Edison, economist, National Federation of Independent Business; accompanied by John J. Motley III, deputy director of Federal legislation 107

Additional material supplied for the hearing record:
- Beck, Carl A., National Small Business Association:
  - Prepared statement 79
  - Report on business bankruptcies 92
- Carlson, Jack, executive vice president and chief economist, National Association of Realtors: Prepared statement with attachments 5
- Cobb, Joe, director of economic analysis, Council for a Competitive Economy:
  - Chart: Money is not tight 62
  - Prepared statement with attachments 44
- McGeady, M. Eamonn, president, Martin G. Imbach, Inc.: Prepared statement 99
- Napolitano, Frederick J., president-elect, National Association of Home Builders: Statement on impact of high interest rates on small business capital formation 30
- Zayas, Edison, economist, National Federation of Independent Business: Prepared statement with attachments 107

APPENDIXES

Appendix A.—Prepared statement of Hon. Christopher S. Bond, Governor of Missouri, including information on effects of Revenue Ruling 81-216 123

Appendix B.—Letters received by Congressman Vin Weber from constituents in response to his request for their opinions 149

IMPACT OF HIGH INTEREST RATES ON SMALL BUSINESS CAPITAL FORMATION

THURSDAY, OCTOBER 15, 1981

House of Representatives,
Subcommittee on Tax, Access to Equity
Capital and Business Opportunities,
Committee on Small Business,
Washington, D.C.

The subcommittee met, pursuant to notice, at 9:30 a.m., in room 2359-A, Rayburn House Office Building, Hon. Henry J. Nowak (chairman of the subcommittee) presiding.

OPENING STATEMENT OF CHAIRMAN NOWAK

Mr. Nowak. The subcommittee will come to order and start today's hearings. I have a brief opening statement and then we'll go right to the witnesses here today.

The present administration's plan for economic recovery includes tax cuts and budget cuts while the Federal Reserve Board steadfastly holds to its tight monetary policy. In the midst of these economic policies the collective voice of the small business community is clamoring for relief from high interest rates which have recently been as high as 20 percent.

It cannot be denied that a sound economic recovery plan is crucial to the Nation's economic well-being. Nor can we afford to avoid the responsibility and challenge of controlling inflation, which by itself, can totally drain our economic vitality.

However, all things considered, we must not ignore the bleak economic realities which now face our small business community. Persistent high interest rates have been devastating to the small business person and have caused severe recessionary trends in terms of bankruptcies, plant closings and layoffs in the interest-sensitive sectors of our economy.

The automobile dealers have reported that they are in a severe depression. Since consumers cannot finance auto purchases at today's high interest rates, automobile dealers are closing their doors at record levels.

Home builders and realtors have been suffering dramatically under the present interest rate levels, as evidenced by the fact that new construction of single family units was at its lowest monthly rate in August since 1975. In addition, Dun & Bradstreet statistics indicate that business bankruptcies have increased over 40 percent in 1981 from the comparable period in 1980.

Admittedly, our country is faced with conditions where everyone must share in the burden of economic restraints but we cannot allow an economic scenario which threatens to irreparably harm our small business community, the cornerstone of our Nation's economic stability.

With these thoughts in mind, let us welcome today's witnesses.

With us in the first panel will be Dr. Jack Carlson, who is the executive vice president and chief economist for the National Association of Realtors. Prior to that Dr. Carlson was Assistant Director of the Office of Management and Budget, Assistant Secretary of the Department of the Interior, vice president, and economist for the U.S. Chamber of Commerce.

Frederick Napolitano is a builder-developer from Virginia Beach. He is the president-elect of the National Association of Home Builders and will take office in January 1982. He has been a builder and a successful one for over 30 years. So, gentlemen, with those credentials, I think he'll be able to shed great light upon this problem.

Mr. Carlson, if you'd like to begin.

TESTIMONY OF JACK CARLSON, EXECUTIVE VICE PRESIDENT AND CHIEF ECONOMIST, NATIONAL ASSOCIATION OF REALTORS

Mr. Carlson. Thank you very much, Mr. Chairman. On behalf of the 700,000 members of the National Association of Realtors, we appreciate the opportunity to talk on this vital topic.

As you noted, Mr. Chairman, the interest-sensitive part of the economy is being hurt rather badly, disproportionately so. In the case of housing, which, as you stated is one of those areas that's hit the hardest, I can draw your attention to page 9 of our prepared testimony that shows that the situation that has prevailed during the last 34 months is the most devastating time we've had in the post-war period—five times worse than any other period of time that we've had. Five times worse as the next worse period of time which was 1973 to 1975.

Two and a half million families have been thwarted in their efforts to upgrade housing because of these high interest rates and their impact on the economy. This is the deepest and the longest period of bad times that have existed in servicing homeowners throughout the Nation. And it's just not a problem dealing with housing for shelter purposes and as an investment medium. Those areas are very important, and certainly in the case of shelter, we're not taking care of the people that are now forming new households of their own and we're falling behind in taking care of that need—falling behind considerably. Because of that, we're going to find out that in the future, we will not have the housing when the demand comes into the market, and then we'll have more inflation, not less inflation. So it's a very bad anti-inflation policy.

But it's just not the shelter side and it's just not the investment side, it's also more fundamental. And where it's more fundamental it strikes at our system in our country for dispersing decision-making and that's through homeownership, as two-thirds of Americans, roughly, own their own home. When they own their own home they get to determine how that home is used and also they're vitally interested in the street that goes in front of their house, the sewer connection and all the other social overhead items that are provided by the community.

They become very interested and a very major part of our decisionmaking. When you do not have homeownership you have less interest and consequently, less dispersal of decisionmaking.

So, to the extent that we're making it impossible for the next generation to have their own housing, we're also undermining our dispersal of decisionmaking; we're undermining democracy itself.

As a result of high interest rates we're already finding out that in order to attract workers to areas, firms have to provide housing. I just came from a meeting with the Senate Finance Committee and we had Senator Wallop and people from Wyoming there, indicating that the energy firms are also finding out they have to provide housing. So we're going back to the employer providing the housing as opposed to the individual owning housing. And you can imagine the leverage effect that that will have if that becomes pervasive across the country, and how that can undermine democracy itself.

Also, there's considerable talk that centralized financial institutions will end up owning parts of homes. Shared appreciation mortgage is one way to do that, thereby diluting homeownership and thereby dispersal of ownership. I'm afraid to say that in a few years when the Government finds out that it's abandoning its current housing policy without having a substitute, the Government will run to be of assistance and it may well get into the ownership business and thereby dilute democracy through that mechanism too.

So I do think we're talking about something just beyond shelter, even though shelter is 36 percent of the gross national product. A very large part of our purchases as consumers in this country goes for shelter. We're talking about something so basic as democracy itself. And so we're concerned about that.

Also we're concerned about high interest rates as they disproportionately impact upon small business in general. In fact, because of the high interest rate approach that we've used in our economic policy, we've created an incentive for mergers that would otherwise not have had that incentive to take place.

The current administration has chosen to say that conglomerate mergers and vertical mergers are acceptable. And by the way, I would say that this is the first time since the enactment of the Sherman Antitrust Act that the administration has said that vertical integration is appropriate. There has been general frowning on it, but not an explicit policy that it's bad for the health of the economy.

But when you have these large, merged institutions and maybe just a few dozen of them spanning many industries or many parts of the consumer's market basket, the economic power that goes with that is tremendous. Consequently, I think that in the future it will make it very difficult for small businesses to survive under those conditions because a concentrated firm, a conglomerate firm, a vertically integrated firm need but just sneeze to put small business in his competitive areas out of business. By sneezing, I mean running the price for the service down fairly low for a couple of months can put out the small business and then raise the price to a higher level to recapture those losses in the future.

So I do think we have a problem here with high interest rates creating an incentive to merge and the current Government accepting mergers as a way of life, thereby undermining small business in its opportunity to serve. Except for the high interest rates, in many of the areas we see mergers taking place, I don't see any inherent technological factors or lower unit cost, economies of scale, that would dictate that those mergers are wise on behalf of a lower unit cost for the consumer.

And so this high interest rate is leading us into a raft of economic concentration so that when these interest rates inevitably come down we'll be worse off from a consumer's standpoint, from the competitive standpoint, from a small business standpoint, from the lowest cost for the consumer standpoint. I think one has to be very worried about what's happening in the merger area, in that conglomerate vertical mergers are looked upon with favor at the present time; only the horizontal mergers are looked upon with disfavor at this particular point in time.

Now, to address the interest rates side, we've made recommendations as to what can be done and I do have these in my text on page 4, and if it's all right with you, Mr. Chairman, I'll continue to just talk if I can put my prepared text in the record.

Mr. **Nowak**. Fine. The complete text will be, without objection, put into the record.

[Mr. Carlson's prepared statement with attachments follows:]

PREPARED STATEMENT OF JACK CARLSON, EXECUTIVE VICE PRESIDENT AND CHIEF ECONOMIST, NATIONAL ASSOCIATION OF REALTORS

I am Jack Carlson, Executive Vice President and Chief Economist of the NATIONAL ASSOCIATION OF REALTORS®.

On behalf of the nearly 700,000 members of the National Association, I greatly appreciate the opportunity to present our views on the impact of high interest rates on small business and join with others to petition our government to bring interest rates down by adhering to a budget not to exceed $695 billion in FY 1982 and through a policy which would relax restrictions on money growth.

A great deal has been written and spoken about the devastating effects high interest rates are having on our economy as a whole, but no component of our economy is feeling the devastation as deeply as small business, particularly the housing industry.

Hundreds of thousands of people are unable to achieve what only a few years ago was considered an integral part of life in this democracy -- home ownership. Literally millions of people are unable to qualify for residential mortgages because of interest rates near or above 18 percent.

And many people feel helpless to do anything. The Federal Reserve Chairman has adamantly refused to relax excessively tight money growth restrictions in spite of calls from virtually every sector of the economic community. We do not desire loose monetary growth which would fuel inflation, but like Secretary of the Treasury Donald Regan, we believe a modest increase in money growth will help get interest rates down to levels which will enable housing and the economy to recover and also continue to cover inflation rates.

The debate concerning high interest rates is particularly important because housing costs are such a relatively large part of the economy, approximately 36 percent of GNP, and because of the resulting impacts on the consumers served by small business and on other small businesses.

We estimate in the housing industry that, because of high interest rates, less than 10 percent of first time homebuyers can qualify for a mortgage on the median-priced home. As a direct result, families are unable to upgrade their housing and cannot relocate to seek better employment opportunities. The small businesses serving the industry are also affected: more than 300,000 construction jobs have been lost during the latest recession and hardware stores, paint stores, attorneys, accountants, landscape firms, moving companies and others have seen their business decline and 190,000 jobs have been lost in those industries because of the affordability problem in housing caused by high interest rates.

When the impact of high interest rates on the small business community as a whole is assessed, the results are even more profound. It is estimated that over one and one-quarter million people have lost their jobs during 1981 because of the adverse impacts of high interest rates and the resulting downturn in economic activity.

The high interest policies that have been directly followed have been compounded by policies that indirectly impact on credit availability for small business.

Statements about anti-trust policy by Administration officials have emphasized the intention to focus on horizontal mergers in the same market and to sharply reduce or abandon concern about vertical and conglomerate mergers. This major change in policy away from concern for the potentially anti-competitive effects of vertical and conglomerate mergers seriously disturbs us because of its foreseeable potentially adverse effects on the large number of small business that make up the bulk of the organizations engaged in real estate.

Our concerns are heightened because of the potential lessening of access for smaller firms to loanable funds that could result from vertical mergers that include financial institutions. Access to financial and credit sources is, of course, the life blood of all real estate activities, and any impairment in the competition among and access to these institutions has to be a major concern.

As businesses respond to such policy changes and become larger and more concentrated, pressures build to make government bigger to deal with these effects.

The recent emphasis on strengthening our defenses also adds a relative disadvantage to smaller business, since the major procurement increases involve primarily the larger companies. This apparently inevitable tendency of the Defense Department's major procurement, which favors bigness, adds to the difficulty we feel in obtaining an appreciation for the problems of our members as they are impacted by such things as a policy shift away from concern about vertical and conglomerate mergers.

We do not believe that selective recession in a few industries, which have resulted in as much as a 50 percent drop in economic activity, is either a necessary or an efficient way to achieve the goals for the nation's economy. We question seriously whether this disproportionate distribution of the costs of achieving a better economy can be allowed to continue.

In order to lower interest rates and to respond to the needs of all sectors of the economy we recommend the following:

(1) The President and the Congress should make good on their commitments early this year to hold spending to $695 billion for FY 1982, instead of busting the budget by $10 billion announced by the Administration in July, and a likely further $10 billion as the result of bad initial spending estimates and the appropriations process in the Congress.

(2) If appropriate spending restraint proves unlikely because of inadequate leadership or courage to trim defense, non-defense and/or entitlement programs, then the across-the-board 10 percent personal income tax rate cut scheduled for July 1, 1982, should be deferred for 90 days until October 1, 1982, and the same action may be needed on the July 1, 1983, tax rate cut.

(3) Whether by spending cuts or tax relief deferral, the deficit should not exceed $42.5 billion in 1982 and decline in 1983 to a balance in 1984.

(4) We urge the Congress to encourage the Federal Reserve Board (a) to adopt a slightly less restrictive but non-inflationary monetary policy, including raising the target rates for money and credit growth by one full percentage point, (b) to adopt a secondary, consistent interest rate target range, such as 13 to 16 percent for short-term rates, to reduce excessive fluctuations in rates which alone have accounted for one-fourth of the decline in the interest-sensitive sectors of the economy.

> See Attachment 1 for additional housing starts and sales of existing homes for each state from the above four recommendations.

(5) We urge the President and the Senate to appoint and confirm a qualified small businessperson from the interest-sensitive industries as the next replacement to the Federal Reserve Board, expected January, 1982.

(6) We urge the Congress to insist upon implementatation of the All Savers Certificates including the Congressionally mandated tie that three-fourths of the net funds go for housing and agricultural loans (see Attachment 2 for potential benefits).

We are concerned with the failure of the President and the Congress to stand by their commitments made in the President's March 10 budget revisions and in the Congress's First Concurrent Budget Resolution for 1982. The record to date and the current outlook for 1982 budget spending, as shown in Table 1, shows that budget-busting and deficit-increasing priorities have not departed from Washington, D.C.

TABLE 1

OVERRUNS IN FEDERAL SPENDING CONTRASTED
TO PRESIDENT'S ORIGINAL COMMITMENTS
(Dollars in Billions)

Fiscal Year	January Budget	Actual Budget Spending	Spending Overrun	
			Percentage	Amount
1972	$229.2	$232.0	1.2	$ 2.8
1973	246.3	274.1	11.3	27.8
1974	268.7	269.6	0.3	0.9
1975	304.4	326.2	7.1	21.8
1976	349.4	366.4	4.9	17.0
1977	394.2	402.7	2.2	8.5
1978	440.0	450.8	2.4	10.8
1979	500.2	493.6	-1.3	-6.6
1980	531.6	579.6	9.0	48.0
1981	615.8	661.2e	7.4e	45.4e
1982	695.3 (3/10/81)	May 15 (Congress) 695.5e	0.0e	0.2e
		July 15 (President) 704.8e	1.4e	9.5e
		Sept. 10 (CBO) 723.0e	4.0e	27.7e
		Sept. 24 (President) 709.3e	2.0e	14.0e
		Oct. 1 (REALTORS®) 725.0e	4.4e	29.7e
72-82 Average			4.4	18.8

e = estimate

Source: Budgets of the U.S. Government, First Concurrent Budget Resolution 1982, Congressional Budget Office Update, and public statements of the President.

The recommendations listed above are an extension of those we made earlier this year with the concern that if a similar approach was not accepted, rates would be higher, and unfortunately that is what has happened. Our earlier recommendations included:

- tax relief no greater than spending cuts so that the federal deficit would trend downward each year towards balance in 1984
- limit across-the-board personal income tax relief to keep the deficit from rising.

Since that time -

- greater tax relief was enacted than spending reductions, causing the federal deficit to increase not decrease and set record interest rates
- monetary policy has not been eased significantly.

As a consequence the interest-sensitive sectors of the economy are being crippled five times more severely than at any other time in the past 40 years. For example, conditions in the housing industry are severe. The 34 month old housing recession is not only the steepest but also the longest housing down turn since statistics have been gathered on the resale market (see Table 2).

TABLE 2

PERIODS OF DECLINE IN EXISTING HOME SALES
(Seasonally Adjusted Annual Rates,
Millions of Units)

Housing Recession	Peak	Trough	Date of Recovery to the level of Prior Peak	Percent Decline Peak to Trough	Total Duration Peak Through Recovery
1969-1970	Dec. 1968 1,710,000	Mar. 1970 1,370,000	Aug. 1970 1,720,000	-20%	20 months
1974-1975	Feb. 1973 2,500,000	Jan. 1975 2,040,000	Sept. 1975 2,600,000	-18%	31 months
1979-?	Nov. 1978 4,020,000	Aug. 1981 2,260,000	?	-44% so far	34 months so far

Source: NATIONAL ASSOCIATION OF REALTORS®

The housing industry is currently suffering from the deepest recession in post-war history. Housing starts are at a 0.937 million units annual rate currently, and expected to average only 1.2 million units for 1981—virtually the same as last year. We expect only 1.5 million starts in 1982 and 1.5 million starts in 1983. Since the underlying demand for replacement and new housing is about 2 million units per year, housing supply is expected to continue far below the underlying housing demand. The implication is for housing to be in short supply throughout the 1980's as industry capacity will not be able to both supply the growing needs of expected demographic demands and the leftover unsupplied demand of the current housing recession. This will only add to future increases in housing prices and rents, and increased upward pressure on the long-term rate of inflation.

Resale activity has also dropped from its November, 1978, peak of 4.02 million units to a low in August, 1981, of 2.26 million units (see Table 2).

While we have come to regard widespread and rising homeownership as a given, the severe depth and duration of the current and continuing recession in home sales raises a profound concern that we believe needs to be identified and addressed. It is worthy of our most responsible and courageous political actions, in the highest meaning of that maligned word "political."

The cumulative losses of home sales in the current recession are greater than in any previous recession. The data are shown in Table 3.

TABLE 3

CUMULATIVE LOSSES OF EXISTING HOME SALES
DURING TIGHT MONEY PERIODS

Tight Money Periods	Duration of Sales Cycle (Peak to Recovery)	Percent Decline in Existing Home Sales (Peak to Trough)	Unit Volume of Sales Lost	Dollar Volume of Sales Lost (In Billions of Dollars)
1969-1970	21 months	-19.9 percent	236,000	$ 5.7
1973-1975	32 months	-18.4 percent	489,000	$ 17.4
1979-1981	34 months (so far)	-43.8 percent	2,494,000	$175.6

Source: NATIONAL ASSOCIATION OF REALTORS®

The American view is clear that widespread homeownership ensures democracy. This comes about by the fact that homeownership disperses decision-making to each individual household over the use and protection of the individual home. Each individual homeowner quite naturally has a stronger incentive to assure success and good conditions in the neighborhood, the community, town or city. Thus the fact that two-thirds of the nation's occupied housing units are owner-occupied is a basic reason that democracy is more of a fact in the United States than elsewhere in the World. This view is not new and is the foundation on which national housing policies since the 1930's have been erected. This view was again documented in the recent national survey conducted during August, 1981, by the Cambridge Surveys, Inc. and commissioned by the NATIONAL ASSOCIATION OF REALTORS®. In that survey, 71 percent of all respondents agree with the statement that widespread homeownership ensures greater democracy. Widespread agreement cuts across all regions, all age groups, and all income levels. These data, which confirm the importance in our national set of values of homeownership, underscore the profound importance of the current, prolonged, and continuing recession in housing. They are shown in Table 4.

TABLE 4

ATTITUDES OF PUBLIC ON WHETHER OR NOT WIDESPREAD HOMEOWNERSHIP ENSURES GREATER DEMOCRACY

(Percentage Distribution)

	Agree	Neither Agree Nor Disagree	Disagree	Don't Know
Total United States	71	8	12	10
Less than $10,000 Income	61	9	12	18
$10,000 to $19,999	67	8	16	10
$20,000 to $34,999	76	7	10	8
$35,000 and over	81	8	8	3
25 years of age and under	65	11	17	10
26 to 45	75	11	13	10
46 to 65	76	5	10	9
over 65	73	5	9	13
Northeast	72	10	9	9
Industrial	63	8	15	13
Midlands	72	10	10	8
South	75	5	10	10
Central	73	13	11	4
Pacific	73	4	9	13

Source: Cambridge Reports, Inc. for NATIONAL ASSOCIATION OF REALTORS®

The basic cause of the severe conditions described in Tables 2 and 3 is the excessive reliance on monetary policy, rather than relying on monetary policy used in conjunction with an equally restrictive fiscal policy. We agree that an effective anti-inflation program requires a long-term policy reducing growth in money and credit over time to rates consistent with the growth of output and employment at stable prices.

However, a less restrictive monetary stance and a tighter and better directed fiscal policy with reducing deficits would more evenly and fairly place the burden of fighting inflation, would be more effective in lowering inflation and interest rates, would better encourage investment in housing and industry, would prevent a renewal of long run inflation in the future from capital and housing shortages, and would lead to strong growth overall.

The consequences of increases in the deficit are basically that they would be financed by reductions in private credit of which, by experience, about one-fourth is for housing.

Because of this crowding out relationship, we are most concerned about the decisions on and estimates of the 1982 deficit. This concern is more severe because of the record in recent years of budget-busting in budget outlays from the January-March date when the President presents a budget, until about 20 months later when the actual spending is known. We would plead for reform to prevent repeating this record. While we believe that sufficient spending reductions can and should be made, we realistically recognize such action is not assured, and further that unanticipated spending increases tend to exceed budgeted amounts.

For the above reasons we have proposed that if the President and the Congress believe the necessary spending cuts are impossible, they must—to reduce the deficit to bring down interest rates—defer the 10% across-the-board reduction in individual income tax rates from July 1, 1982, to October 1, 1982, and do the same in 1983. We believe that delay of dates for tax relief is an appropriate kind of action to be taken as part of the Second Budget Resolution, as part of the adjusting actions needed in light of the various spending and revenue actions that have been taken since the First Budget Resolution and the Omnibus Budget Reconciliation Act.

ATTACHMENT 1

IMPACT OF $20 BILLION LOWER DEFICIT IN FY1982, DECLINING TO BALANCE IN FY1984 AND A 1 PERCENT FASTER RATE OF GROWTH OF THE MONEY SUPPLY ON HOUSING STARTS AND SALES

(Units)

	1982			1983			1984		
States	Starts	Existing Home Sales	Total Housing Activity	Starts	Existing Home Sales	Total Housing Activity	Starts	Existing Home Sales	Total Housing Activity
U.S. Total	100,000	200,000	300,000	215,000	425,000	640,000	330,000	750,000	1,080,000
Alabama	1,700	3,820	5,510	3,680	7,940	11,620	5,650	14,000	19,660
Alaska	250	370	620	620	700	1,320	950	1,230	2,180
Arizona	2,880	3,600	6,480	6,550	8,070	14,630	10,060	14,250	24,310
Arkansas	1,100	2,530	3,630	2,370	5,320	7,690	3,640	9,380	13,020
California	12,210	19,640	31,850	27,160	39,950	67,110	41,680	70,500	112,180
Colorado	2,390	3,080	5,470	5,500	6,970	12,480	8,450	12,310	20,760
Connecticut	730	1,940	2,680	1,540	4,090	5,630	2,370	7,210	9,580
Delaware	220	520	740	460	960	1,420	700	1,700	2,400
Dist. of Columbia	160	250	420	350	530	880	540	930	1,470
Florida	10,640	14,780	25,410	20,490	28,550	49,050	31,460	50,390	81,840
Georgia	3,620	6,660	10,270	7,450	12,890	20,340	11,430	22,760	34,190
Hawaii	530	600	1,130	1,150	1,420	2,570	1,770	2,510	4,280
Idaho	500	870	1,370	1,160	1,890	3,050	1,770	3,340	5,110
Illinois	2,300	7,430	9,730	5,090	17,390	22,480	7,810	30,680	38,490
Indiana	2,050	5,030	7,080	4,250	11,960	16,210	6,530	21,100	27,630
Iowa	950	2,590	3,540	2,090	6,090	8,180	3,200	10,750	13,950
Kansas	1,150	2,600	3,750	2,530	6,080	8,610	3,880	10,730	14,610
Kentucky	1,440	3,100	4,540	3,010	6,930	9,950	4,630	12,230	16,860
Louisiana	2,080	3,710	5,790	4,480	7,530	12,000	6,870	13,280	20,150
Maine	480	970	1,450	1,040	1,890	2,930	1,600	3,340	4,930
Maryland	1,500	3,430	4,930	3,070	6,610	9,680	4,710	11,670	16,380
Massachusetts	1,220	3,030	4,250	2,410	6,030	8,440	3,700	10,640	14,340
Michigan	2,420	8,280	10,700	5,320	19,910	25,230	8,160	35,140	43,310
Minnesota	1,680	4,290	5,980	3,710	10,120	13,830	5,690	17,860	23,550
Mississippi	1,030	2,490	3,520	2,190	4,850	7,040	3,360	8,560	11,920
Missouri	1,350	5,260	6,610	2,890	13,060	15,940	4,430	23,040	27,470
Montana	240	540	780	530	1,250	1,780	810	2,210	3,020
Nebraska	680	1,790	2,470	1,560	3,850	5,410	2,390	6,800	9,190
Nevada	940	1,050	1,990	2,290	2,480	4,770	3,520	4,370	7,890
New Hampshire	490	950	1,450	1,120	1,920	3,040	1,710	3,400	5,110
New Jersey	1,860	4,650	6,510	4,080	10,190	14,260	6,260	17,980	24,230
New Mexico	690	1,210	1,900	1,610	2,540	4,150	2,480	4,480	6,960
New York	1,900	7,530	9,430	3,950	15,440	19,390	6,070	27,250	33,320
North Carolina	3,490	5,690	9,180	6,920	11,410	18,340	10,630	20,140	30,770
North Dakota	320	580	900	700	1,450	2,150	1,080	2,550	3,630
Ohio	2,550	8,440	10,990	5,550	20,390	25,950	8,520	35,990	44,510
Oklahoma	1,810	4,050	5,860	4,060	8,290	12,360	6,240	14,640	20,870
Oregon	1,690	2,640	4,330	3,860	5,320	9,170	5,920	9,380	15,300
Pennsylvania	2,380	7,500	9,880	5,000	16,130	21,140	7,680	28,470	36,150
Rhode Island	230	510	740	470	1,170	1,650	720	2,070	2,800
South Carolina	1,710	3,320	5,030	3,640	6,650	10,290	5,590	11,730	17,330
South Dakota	430	780	1,210	1,040	1,610	2,650	1,590	2,850	4,440
Tennessee	1,990	4,440	6,440	4,430	9,230	13,660	6,790	16,290	23,080
Texas	10,210	16,930	27,140	22,250	33,070	55,330	34,160	58,360	92,520
Utah	820	1,080	1,910	1,980	2,580	4,570	3,050	4,560	7,600
Vermont	400	550	950	840	1,010	1,850	1,300	1,780	3,080
Virginia	2,880	5,310	8,180	5,910	10,360	16,270	9,080	18,280	27,360
Washington	3,160	3,950	7,110	7,210	8,450	15,660	11,060	14,920	25,980
West Virginia	410	1,310	1,720	870	2,740	3,620	1,340	4,840	6,180
Wisconsin	1,740	3,840	5,580	3,660	8,660	12,320	5,620	15,280	20,900
Wyoming	400	490	880	890	1,050	1,940	1,370	1,850	3,220

SOURCE: NATIONAL ASSOCIATION OF REALTORS®, Forecasting and Policy Analysis Division.

ATTACHMENT 2

POTENTIAL IMPACT OF ALL SAVERS CERTIFICATES ON HOUSING, EXISTING HOME SALES AND MORTGAGES

States	Housing Starts	Existing Home Sales	Additional Mortgage Funds (Millions)
UNITED STATES	250,000	437,500	$30,000
Alabama	4,700	8,225	564
Alaska	550	962	66
Arizona	6,825	11,944	819
Arkansas	2,875	5,031	345
California	28,950	50,663	3,474
Colorodo	5,075	8,881	609
Connecticut	1,900	3,325	228
Delaware	525	919	63
District of Columbia	450	788	54
Florida	27,900	48,825	3,348
Georgia	8,800	15,400	1,056
Hawaii	1,500	2,625	180
Idaho	1,125	1,969	135
Illinois	6,050	10,587	726
Indiana	4,450	7,788	534
Iowa	2,000	3,500	240
Kansas	2,575	4,506	309
Kentucky	3,375	5,906	405
Louisiana	4,850	8,488	582
Maine	1,025	1,794	123
Maryland	4,125	7,219	495
Massachusetts	3,075	5,381	369
Michigan	6,050	10,588	726
Minnesota	4,850	8,488	582
Mississippi	2,975	5,206	357
Missouri	4,650	8,138	558
Montana	425	744	51
Nebraska	1,825	3,194	219
Nevada	2,175	3,806	261
New Hampshire	1,250	2,188	150
New Jersey	3,775	6,606	453
New Mexico	1,725	3,019	207
New York	5,100	8,925	612
North Carolina	7,975	13,956	957
North Dakota	825	1,444	99
Ohio	6,700	11,725	804
Oklahoma	4,900	8,575	588
Oregon	4,225	7,394	507
Pennsylvania	6,300	11,025	756
Rhode Island	625	1,094	75
South Carolina	4,575	8,006	549
South Dakota	975	1,706	117
Tennessee	5,275	9,231	633
Texas	26,125	45,719	3,135
Utah	2,100	3,675	252
Vermont	600	1,050	72
Virginia	7,100	12,425	852
Washington	7,050	12,338	846
West Virginia	1,200	2,100	144
Wisconsin	5,075	8,881	609
Wyoming	850	1,488	102

ATTACHMENT 3

U.S. ECONOMIC OUTLOOK
(October 1981)

	QUARTERS								YEARS				
	Actual		Forecast						Actual		Forecast		
	81:1	81:2	81:3	81:4	82:1	82:2	82:3	82:4	1979	1980	1981	1982	1983
AGGREGATE ECONOMY													
Gross National Product ($ billions)	2,853	2,886	2,944	3,025	3,105	3,200	3,307	3,416	2,414	2,626	2,927	3,257	3,625
Percent Change	19.2	4.7	8.4	11.4	11.0	12.8	14.1	13.8	12.0	8.8	11.5	11.3	11.3
Percent Change (without inflation)	8.6	-1.6	0.0	1.6	3.4	4.9	5.5	4.1	3.2	-0.2	2.2	2.9	3.2
Consumption	5.8	-2.1	5.6	3.2	3.4	3.7	4.9	4.2	2.9	0.5	3.2	3.6	3.2
Residential Investment	3.2	-22.8	-15.0	-19.0	28.4	38.3	32.9	20.4	-5.2	-18.6	-2.3	10.0	10.9
Nonresidential Investment	13.4	-2.2	0.1	1.1	1.8	14.0	9.5	10.0	6.5	-3.0	1.9	4.9	7.8
Structures	16.6	6.7	-1.3	1.6	0.2	1.0	3.3	6.1	8.7	-0.1	3.7	1.6	4.6
Equipment	11.8	-5.9	0.6	0.9	2.4	20.5	12.3	11.6	5.5	-4.2	1.2	6.3	9.2
Exports	13.6	-2.4	-3.4	-2.2	-1.7	2.5	4.9	6.4	15.2	9.6	-0.2	0.0	6.0
Imports	10.3	14.3	2.5	4.5	5.6	8.4	9.1	9.3	6.0	-0.1	5.5	6.7	7.1
Government Purchases	5.3	-5.5	1.9	-1.5	0.2	0.4	1.5	-3.4	1.5	2.9	0.3	-0.3	-1.0
Consumption (% of GNP)	63.3	63.2	64.1	64.4	64.4	64.2	64.1	64.1	62.8	63.2	63.8	64.2	64.2
Residential Investment (% of GNP)	3.4	3.2	3.0	2.9	3.0	3.2	3.4	3.6	4.0	3.2	3.1	3.3	3.6
Nonresidential Investment (% of GNP)	10.7	10.7	10.7	10.7	10.6	10.8	10.9	11.1	11.0	10.7	10.7	10.9	11.4
Inventory Change ($ billions)	4.5	23.3	0.7	8.8	16.1	19.4	22.4	26.8	17.5	-5.9	9.3	21.2	22.9
Mfg. Capacity Utilization Rate (%)	80	80	80	80	81	82	83	84	86	79	80	82	83
Manufacturing Industrial Production (% change)	7.5	3.0	2.5	5.8	6.9	9.8	9.4	6.4	4.6	-4.5	4.4	6.7	4.8
Employment (millions)	98.0	98.9	99.3	99.4	100.0	100.7	101.3	102.0	96.9	97.3	98.9	101.0	103.7
Unemployment Rate (%)	7.3	7.4	7.1	7.5	7.5	7.3	7.3	7.1	5.8	7.1	7.3	7.3	6.8
Disposable Income per Household (average)	25,251	25,682	26,425	27,155	27,660	28,236	29,379	30,046	21,565	23,748	26,128	28,830	31,803
Percent Change -- Year Ago (w/o inflation)	0.3	1.9	2.0	2.5	2.0	2.3	3.6	3.0	2.2	-0.1	1.7	2.7	2.6
Total Taxes per Household (average)	13,341	13,382	13,563	13,673	14,010	14,380	14,401	14,798	11,106	12,057	13,490	14,397	15,254
Percent Change -- Year Ago	13.3	14.6	12.3	7.7	5.0	7.5	6.2	8.2	10.5	8.6	11.9	6.7	6.0
Household Debt as Percent of Disposable Income	77.9	77.9	76.9	76.0	75.9	75.8	74.4	74.3	80.2	79.3	77.2	75.1	74.1
Consumer Price Inflation (CPI)	10.8	7.5	10.6	9.0	7.8	7.8	8.2	8.6	11.3	13.5	10.2	8.5	8.4
Gross National Product Inflation (GNP Deflator)	9.8	6.4	8.4	9.7	7.4	7.5	8.1	9.4	8.5	9.0	9.0	8.1	7.9
Personal Consumption Inflation	8.0	6.5	8.1	7.5	7.3	7.1	7.5	7.7	8.9	10.2	8.2	7.4	7.5
Residential Construction Inflation	10.1	5.7	6.9	8.9	10.5	10.2	11.1	10.8	12.8	9.4	7.0	9.5	10.0
Nonresidential Construction Inflation	5.1	14.1	7.9	9.8	11.0	10.4	11.6	11.3	12.6	13.4	9.4	10.6	10.7
Producers Price Inflation (WPI)	9.5	8.9	5.6	8.4	8.6	8.8	10.3	10.8	12.5	14.1	9.7	8.6	10.1
Compensation per Manhour (% change)	11.4	9.8	9.3	9.7	9.4	8.9	9.3	9.1	9.7	9.9	10.1	9.4	9.2
Productivity (% change)	4.1	0.8	-2.0	0.8	2.0	1.6	1.6	2.0	-0.7	-0.3	1.2	1.1	1.8
Unit Labor Cost (% change)	6.9	8.9	11.6	8.8	7.3	7.2	7.6	7.0	10.4	10.3	8.8	8.2	7.2
Unit Capital Cost (% change)	10.8	10.4	9.9	9.4	9.0	8.8	8.7	8.7	11.1	11.0	10.1	8.8	9.0
Before Tax Corporate Profits ($ billions)<1>	286	260	249	263	272	290	309	327	255	258	264	300	333
Corporate Tax Liability	88	76	73	78	81	87	94	100	88	82	79	91	99
'Windfall Profits' Tax Receipts	29	31	27	28	28	29	29	30	0	13	29	29	31
Inventory Valuation Adjustment	-39	-24	-28	-30	-36	-38	-43	-47	-43	-46	-30	-41	-49
Capital Consumption Adjustment	-15	-15	-15	-17	-14	-16	-18	-19	-16	-17	-15	-17	-13
After Tax Profits	169	153	149	157	163	174	186	197	168	163	157	180	203
Profits from Current Production (with IVA, CCA)	115	114	106	110	113	120	125	131	109	100	111	122	141
Adjusted for Inflation (81:1 base)	115	112	103	104	105	109	112	114	126	107	108	110	118
Percent Change - Year Ago	-1.1	6.9	-1.8	3.4	-9.0	-2.6	9.2	9.9	-1.6	-15.7	1.8	1.5	7.1
Per Unit of Output (% of GNP)	4.0	4.0	3.6	3.6	3.6	3.8	3.8	3.8	4.5	3.8	3.8	3.8	3.9
Effective Corporate Tax Rate (%)<1>	43	41	41	42	42	42	43	44	45	45	42	43	42
Federal Tax Receipts (Unified basis)	541	735	621	561	566	827	657	617	481	533	615	667	711
Federal Expenditures (Unified basis)	669	670	666	700	717	723	732	754	509	501	676	731	782
Surplus or Deficit (Unified basis)	-128	65	-45	-139	-150	104	-75	-137	-28	-68	-62	-65	-71

<1> Adjusted to include impact of windfall profits tax on domestic crude oil production.

Source: Model developed by the NATIONAL ASSOCIATION OF REALTORS, and Data Resources, Inc.
Assumptions and simulations by Dr. Jack Carlson, [redacted], Kenneth Kerin, and Glenn Crellin.

ATTACHMENT 4

REAL ESTATE AND FINANCIAL MARKETS
(October 1981)

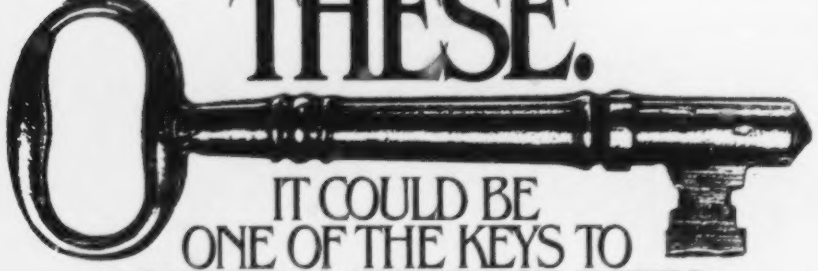
	QUARTERS								YEARS				
	Actual		Forecast						Actual		Forecast		
	81:1	81:2	81:3	81:4	82:1	82:2	82:3	82:4	1979	1980	1981	1982	1983
REAL ESTATE MARKETS													
Existing Single-Family Home Sales (thousands)	2,543	2,600	2,356	2,507	2,693	2,918	3,049	3,222	3,701	2,881	2,502	2,970	3,576
Percent Change - Year Ago	-15.4	5.5	-22.9	-16.3	5.9	12.2	29.4	28.5	-4.2	-22.2	-13.2	18.7	20.4
Dollar Volume (billions)	193.3	204.7	187.6	201.4	218.9	243.6	261.9	279.3	237.6	209.7	196.7	250.9	329.6
New Single-Family Home Sales (thousands)	510	447	383	414	433	425	456	496	709	531	438	455	574
Percent Change - Year Ago	-4.1	-1.2	-36.4	-23.5	-15.1	-5.0	22.4	19.8	-13.2	-25.1	-17.5	3.9	26.0
Private Housing Starts (thousands)	1,391	1,176	976	1,109	1,352	1,466	1,624	1,669	1,745	1,292	1,163	1,528	1,510
Single-Family	874	783	613	706	873	946	1,044	1,066	1,194	852	744	982	993
Multi-Family	517	393	363	404	479	519	580	603	551	440	419	545	517
Subsidized	136	156	155	157	161	163	165	161	120	156	151	163	153
Mobile Home Shipments (thousands)	248	255	223	216	233	254	272	280	276	224	236	260	266
Housing Inventory (millions)	84.2	84.4	84.6	84.7	84.8	85.0	85.2	85.5	82.8	83.7	84.5	85.2	86.2
New Construction Put In Place - (Value)													
New Commercial Buildings (% Change)	54.1	-5.7	7.7	4.0	4.7	6.4	7.3	15.6	33.8	21.7	10.7	5.6	12.9
New Industrial Buildings (% Change)	78.1	12.7	7.5	3.3	9.8	13.2	16.9	20.8	37.2	-6.7	13.6	10.7	19.7
Rental Vacancy Rate (%)	5.2	5.0	5.1	5.0	5.0	5.0	4.8	4.9	5.4	5.4	5.1	4.9	5.0
Unsold New Homes (% of sales)	65.8	73.7	59.0	54.6	51.2	50.8	50.7	52.6	59.3	70.2	63.3	51.3	62.8
Office Vacancy Rate (%)<1>	3.9	4.2	4.2	4.1	4.0	3.9	3.8	3.8	4.4	3.7	4.1	3.9	3.6
Industrial Vacancy Rate (%)<1>	3.8	3.6	3.7	3.8	3.7	3.6	3.6	3.5	3.0	3.5	3.7	3.6	3.4
Existing Home Prices - Median ($1000's)	64.3	66.4	67.8	68.9	70.1	72.3	74.7	75.6	55.7	62.2	66.9	73.2	80.6
Percent Change - Year Ago	9.4	7.7	5.3	8.8	9.0	8.9	10.1	9.7	14.1	11.7	7.8	9.4	10.1
Monthly Mortgage Payment (P&I, 80%, 30 yr.)	667	721	784	740	710	711	741	761	433	588	728	731	793
Percent of Household Income	27	28	30	28	26	25	26	26	20	25	28	26	26
New Home Prices - Median ($1000's)	67.2	69.5	70.6	72.1	74.2	76.4	78.8	81.1	62.7	64.9	69.9	77.6	86.5
Percent Change - Year Ago	5.6	9.5	7.3	8.4	10.4	10.0	11.6	12.4	12.5	3.4	7.7	11.1	11.4
New Home Prices--Mean ($1000's, Quality Adjusted)	83.3	85.1	86.0	90.0	92.9	93.2	94.1	98.5	71.4	78.5	86.1	94.7	103.4
Percent Change - Year Ago	10.3	8.5	7.5	12.1	11.5	9.5	9.4	9.4	14.8	10.1	9.6	10.0	9.2
FINANCIAL MARKETS													
Total Time and Savings Deposits (% change)	13.1	3.1	6.0	5.9	7.7	9.9	10.9	11.4	8.6	7.5	8.6	7.9	9.8
Savings Rate (%)	4.6	5.4	5.2	5.4	5.1	5.3	5.4	5.5	5.3	5.6	5.2	5.3	5.6
Money Supply (M1B) (% change)	5.0	9.1	1.4	8.4	4.1	4.1	3.2	4.9	7.8	6.3	7.3	5.5	4.9
Money Supply (M2) (% change)	6.5	11.0	8.7	9.4	5.4	7.1	10.2	9.8	8.[illegible]	9.0	9.9	8.1	8.5
New Mortgage Commitments ($ billions)	72.7	69.3	70.5	63.7	73.6	81.3	85.8	89.6	129.0	88.0	69.1	82.6	95.7
Percent Change - Year Ago	-10.4	48.4	-41.9	-37.9	1.2	17.2	21.8	40.7	-9.2	-31.8	-21.5	19.6	15.8
Mortgage Debt Outstanding ($ billions)	1,475	1,497	1,535	1,564	1,596	1,627	1,657	1,693	1,266	1,401	1,518	1,643	1,786
Homeowners' Equity ($ billions)	2,835	2,911	2,969	3,037	3,124	3,212	3,318	3,437	2,618	2,759	2,938	3,273	3,735
Selected Interest Rates (Percent)													
New Home Mortgage Commitment Rate	15.40	16.16	17.25	15.98	15.02	14.55	14.69	14.92	11.27	14.00	16.19	14.80	14.58
Corporate Bond Rate (AAA)	13.16	13.98	14.62	14.67	14.60	14.56	14.55	14.40	9.63	11.94	14.11	14.53	13.44
Rate on Money Market Fund Shares	15.67	16.51	17.21	15.49	16.45	16.38	16.00	16.22	11.12	12.89	16.22	16.26	16.49
Commercial Paper Rate	15.34	16.15	16.75	15.26	15.62	15.24	14.97	15.37	10.97	12.66	15.87	15.30	16.22
Prime Rate	19.21	18.93	20.21	17.84	17.54	17.47	17.23	17.02	12.67	15.27	19.05	17.31	16.32
Federal Funds Rate	16.57	17.78	17.47	15.21	15.76	16.19	15.99	16.23	11.19	13.36	16.76	16.04	17.10

<1> Historical data courtesy of Coldwell Banker.

Source: Model developed by the NATIONAL ASSOCIATION OF REALTORS, and Data Resources, Inc.
Assumptions and simulations by Dr. Jack Carlson, Hugh Graham, Kenneth Kerin, and Glenn Crellin.

ATTACHMENT 5

SEND CONGRESS ONE OF THESE.



IT COULD BE ONE OF THE KEYS TO LOWERING INTEREST RATES AND UNLOCKING THE ECONOMY.

Why send a key to Congress? To dramatize your frustration with an economic policy that keeps interest rates high.

These three proposals, we feel, could be the latchkey that opens the way to a healthy economy.

1. The President and the Congress to hold the budget deficit to under $42.5 billion in fiscal 1982. Balance the budget in fiscal 1984.

2. The Federal Reserve Board to allow the money supply to increase at the upper end of its monetary targets to accommodate economic growth and stability.

3. The President to appoint a non-banking, small-business representative to fill the first vacancy on the Federal Reserve Board.

The Administration, the Congress, the Federal Reserve Board can no longer ask the public to accept the economic hardships resulting from the devastating cost of money.

It stifles economic growth. It increases the deficit. It reduces employment. It prevents expansion. And it depresses national spirit.

To:

☐ **The Honorable**
U.S. Senate
Washington, DC 20510

☐ **The Honorable**
U.S. House of Representatives
Washington, DC 20510

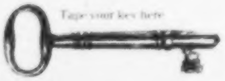
Here's my key to a healthy economy and lower interest rates. I want my feelings known.

Name

Address

City State Zip

Tape your key here



You can show how you feel about high interest rates by sending a key to your people in Congress. Any key will do. A house key. A car or a truck key. An office key.

These keys signify the ravages of tight money and high interest rates. Your key would be symbolic of the home you couldn't buy. The new car or truck you needed but had to put off buying. The bankrupt business whose doors you were forced to close.

So send Congress your tired, your battered, your worn-out keys. Attach yours to the coupon below and send it to Congress today. Your cooperation may be the key to lower interest rates.

National Automobile Dealers Association.
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Elected Officers are: President John R. Wood, Naples, Florida; President-elect Julio S. Laguarta, Houston, Texas; Treasurer Budd Krones, Tucson, Arizona.

The Chief Administrative Officer is Jack Carlson, Executive Vice President and Chief Economist.

The Senior Vice President, Government Affairs is Albert E. Abrahams and the Vice President and Legislative Counsel, Government Affairs is Gil Thurm.

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Mr. CARLSON. We've supported the Congress in the First Concurrent Budget Resolution and the President in his March statement to keep the budget at $695 billion.

Having spent nearly a decade as Assistant Director of the old Bureau of the Budget in the Office of Management and Budget, I like to follow these things rather closely and I'm afraid that budget busting, as usual, prevails. The President announced the first explicit budget busting in July of this year in the mid-year update from $695 billion to $705 billion. And the Congress, not to be outdone, I understand, through the appropriations process, another $10 billion was busted.

According to David Stockman, instead of $695 billion, we're now running at $720 to $725 billion. It's interesting to note that that $720 to $725 billion in relationship to $695 billion is the average busting of the budget during the last 10 years.

So I don't think one can claim that there's been a significant change on what was stated in first concurrent budget resolutions or in the President's message at the first of the year in terms of where we find ourselves with the spending for this particular fiscal year.

For those that like to follow that sort of thing, I do have a table in the text that shows explicitly what the budget busting was of every other President and Congress during the last 10 years. The average was 4.4 percent budget busting and our estimate at the current time, and evidently vouched by Mr. Stockman, is at 4.4. So it's business as usual on the spending side. And we're concerned about that.

We're, in fact, saying that if we cannot handle it on the spending side, as apparently we are not handling it, and we're running into problems with further cuts, we would recommend as a second-best solution, deferring personal income tax cuts scheduled for July 1, 1982, to October 1, 1982, and perhaps the same action for the personal income tax cuts scheduled for 1983. Deferring the cuts for 6 months will give you $10 billion off of the deficit in fiscal year 1982 and $20 billion off the deficit in fiscal year 1983.

We think it's imperative to bring down that deficit from what we think is running at $63 billion to get it to $43 billion and have it go down to a balance by 1984. And quite frankly speaking, the people that we represent, homebuilders and other owners of real property, for every $10 billion increase in the deficit, $2½ billion comes out of home mortgages, and that's equivalent to 100,000 home sales, opportunities for families to upgrade themselves. And so we thwart the wishes of 100,000 families every time the deficit goes up $10 billion and the Government borrows that money and takes it away from loanable funds that would have otherwise gone into mortgages. So we're very concerned about bringing the deficit down to $43 billion in 1982 and toward a balance in 1984.

Quite frankly speaking, we were pleased to see the repentance of the Federal Reserve Board in October of 1979, that they became part of the solution instead of part of the problem. However, that repentance has gone too far and in their zeal, money policy has become too tight from our standpoint—we would argue 1 to 2 percentage points faster growth of money supply, whether you're talking about M1B or M2 or any other figure you're talking about. A modest, only a modest increase in the money supply, is justified to take the proportional burden off of the interest sensitive sectors of the economy and the small business sector of the economy.

Our analysis, which is just as accurate as the Fed's, and unfortunately, there's a lot of difficulty in being accurate in this area, is that we can bring down the inflation rate. Yet taking the heavy burden of fighting inflation solely through high interest rates, which we have, actually stimulates fiscal policy, and keeps the deficit climbing, and we therefore have a perverse mix of policies at the present time.

In fact, it's interesting to notice that our Representatives who represent the American people in the Congress and with the President are the ones guilty of stimulating the inflation leading to the higher interest rates as opposed to the nonelected Federal Reserve Board that tends to be too energetic in fighting inflation alone. Consequently, the interest rates are too high.

We would also argue with the Federal Reserve Board that they should not increase the supply of money, but they ought to use the secondary objective more explicitly of having an interest rate range that they would support—maybe 13 to 16 percent by some short-term interest rate measure—would be the zone that they'd like in addition to their 3½ to 6 percent on M1B or any of the other growth measures.

The reason for that is that we found that one-third of the loss of opportunity for people to upgrade their housing in 1982 came from the fluctuation of interest rates. Two-thirds came from the average height being much higher on the average interest rates. So the fluctuation creates uncertainty alone. So we would argue that policies ought to stabilize the interest rates fluctuations as well as bringing down the average.

We're a little bit concerned that because, disproportionately, the folks that run Federal Reserve policy all come from the same academic mold, the same philosophical training mold, and we think that that body is really affecting the entire economy and there ought to be representation from small business people, from the interest sensitive sector of the economy, obviously knowledgeable people, that should serve on that Board. So we recommended to the President that his next appointment—and his opportunity will come up in January of 1982—should be a small business person from the interest sensitive sector of the economy and not out of the mold that almost all of the current members find themselves, which is primarily an academic, heavy governmental service mold, as opposed to a private sector, small business mold.

We're very much concerned too that the existing tax law is carried out. There are certain features that help small business. There is the one feature that, in particular, is aimed at the housing industry and the savings and loans, and that's the all-savers certificate.

We think from the data that we see that the intent of the Congress may well be carried out. I would expect now $150 to $200 billion of funds to flow into those. But I would expect three-quarters of those funds to come from the churning within banks and thrifts. So you get down to about $50 billion that will be net new money and three-quarters of that is mandated by the Congress to go to mortgages and to farm loans.

That's about $37½ billion. That's about 40 percent of the net new mortgages that one can expect in the housing industry. And clearly those funds coming from that source can be 2 percentage points lower. That can be quite helpful.

Now, the other growth funds, not the $50 billion, but the $150 billion that is just churning from higher cost funds within banks and thrifts to lower cost funds, will be available for small business, in fact, for all business. And those funds will be at 3 to 4 percentage points lower cost. So I think the all-savers certificate is one of the best opportunities for lowering interest rates across the board, let alone, that less than 20 percent of the funds that we would expect, if the intent of Congress is carried out, would flow to mortgages and farm loans.

Now, Mr. Chairman, these are our concerns. I would just add the last one in terms of the conglomerate merger and vertical merger. I think that antitrust policy has to be revised and it may well be something different than the current interpretation by the Assistant Attorney General in the Government and by several of the people in the administration who tend to be encouraging merging, bigness, as opposed to supporting smallness and competition.

Thank you, Mr. Chairman.

Mr. NOWAK. Mr. Carlson, thank you very much for your oral testimony and for a very extensive and complete and, I think, very informative statement with the attachments.

I believe we really can get into the detail that you based all of your findings and conclusions on. I think you're absolutely right when you talk about the housing industry as something more than another salable product because, the basis of our whole society, that is, the American dream, is to own your own home. That dream, I think, is not a selfish one. I think it provides a stability and leads to many other positive statements and commitments to a community.

Let me ask you a couple of short questions. I know you are on a very tight schedule and if necessary I will write any additional questions out to you, and perhaps you can send them back for the record. That would be greatly appreciated.

But let me just talk about a couple of things. When we looked at the inflation rate and the interest rate relationship over the years, it was brought to our attention that there's never been such a disparity between the inflation rate and the interest rate. I wonder if you could comment on that.

It would seem in the fifties and sixties when we had terrific growth and terrific homebuilding and purchase opportunities that if the inflation rate was 4 or 5 percent, the interest rate may have been 6 or 6½ percent. And that relationship stayed very close to the inflation rate until the last couple of years. I wonder, is there any new phenomena that you could attribute that to?

Mr. CARLSON. That's a very interesting phenomenon that has occurred. The real interest rate that has been necessary to attract people to save and invest on a longer term basis, whether it's in corporate triple A bonds or whether it's been in mortgages, has been roughly 3 percent above the underlying inflation rate.

The underlying inflation rate, most people would estimate at 9 to 10 percent at the present time. That would mean the interest rate on mortgages should be at 12 to 13 percent. But the published rates are anywhere from 17 to 19 percent at the present time.

There are a number of reasons. One is that we've never had a perversion of economic policy at this particular point in the business cycle in our history that I know of, where we have the size of the deficit, actually increasing and stimulating the economy at the same time that we've had monetary policy tightening down so tight. And consequently, the mix of economic policies is a sure way to get high interest rates and a sure way to clobber small business and the interest sensitive part of the economy.

Second, it has been the great uncertainty that has built up over the years where the investment community, those that take a risk, have listened to comments about ideals or directions or commitments, and the commitments weren't delivered on, the ideals weren't achieved or whatever.

And now the people who take the risks are interest sensitive, they're trigger happy. They're worried about protecting their savings in case there's going to be wide swings in interest rates and inflation rates.

Consequently, you can have a mere announcement of the Federal Reserve Board on the money growth on a Friday afternoon and you can have interest rates change a full percentage point by the next Monday afternoon, which is unusual. So people are uncertain about the future and consequently, we have a trigger happy community. We need to remove that uncertainty.

And then, the other point that I mentioned is that the economic policy is a bad mix of policy for the small business and the interest sensitive part of the economy.

Mr. NOWAK. Thank you very much. Let me yield to Mr. Marriott, who has some questions. And I would just make the reference to the time that you'll have. We'll have to be through with the questions by approximately 10:15 a.m. for Mr. Carlson's next appointment. So, with that admonition, I would like to recognize Dan Marriott.

Mr. MARRIOTT. Jack, good to see you again, as usual. Let me just ask a couple of questions. And I will be brief.

We have a policy now of cutting the budget and also giving the biggest single block of tax cuts in the history of the country.

Some argue that those two combinations alone, even though they're good in the long run, are going to have the effect of holding interest rates up.

Can you comment on that? Can we realistically bring the interest rates down with that type of policy?

Mr. CARLSON. Clearly, and as we argued before the cuts, spending reductions should have been equal to the tax cuts. And clearly, even the intent was to have the tax relief larger in 1983, 1984, and beyond.

And it looks like even this year when we're through with the year the spending cuts will not be as large as the tax relief. The tax relief will be larger. So in every year we'll have the measures resulting in an increase in the deficit.

So I do think from the standpoint of a high interest policy, we've guaranteed it by our spending and tax policies. That we're going to have higher interest rates than we've ever had, even after you adjust for inflation, during the foreseeable future.

In addition is the uncertainty factor. It is true that with a deficit of $63 billion and a $3 trillion economy, people should not, based on that history, be so trigger happy.

But over 15, 20, or 30 years, really 15 years, since the middle 1960's people have become more and more trigger happy. And so the symbolism of the deficit, even though as a proportion of GNP it's not as large as we've had in the past, is assuming more importance.

As to how to allay those fears, I think the only way is not by pronouncements but by deeds. People are looking at what people are doing as opposed to what they're saying now. And no matter how effective a President is on TV, I am afraid people are looking at their own condition and they want to see results as opposed to expectations or hopes or dreams or commitments, before they're willing to change their investment pattern and be less trigger happy.

I think we have no choice but to work toward that deficit going down because of that environment.

Mr. MARRIOTT. So you would put the emphasis on a balanced budget before any tax cuts. So, as you said earlier, you would prefer to see the tax cuts delayed, the emphasis put on spending cuts, to send the proper signals to the private sector. Is that what you're proposing?

Mr. CARLSON. We will propose to slow down the growth of spending. But in the judgment of people that are in a position to see the whole menu of opportunities, if the cuts cannot be made to get the deficits, the second choice is to defer the personal income tax.

In terms of the housing area, we've made the calculations that deferring the personal income tax cut by 90 days is worth five times more than the loss of the tax relief during that 90 days that would otherwise occur because all business is in the interest sensitive parts of the economy.

So in any case, getting down that deficit, even if you have to defer personal income tax, is going to be five times more important to small business than going ahead with the personal income tax cut on time.

Mr. MARRIOTT. One final question. We are toying around here with the small business participating loan or participating debenture concept of providing alternative sources of capital for small business by giving inducements to investors to invest in small business.

I'm not sure if you understand exactly how the program works. But does such an alternative source of capital idea have any appeal to the home market?

Mr. CARLSON. Dan, I apologize for not knowing specifically the proposal that is before the Congress at the present time, but clearly, any step that is going to provide assistance will have appeal.

Now in the longer run credit allocation can lead to prepared credit controls and I think that you have some perverse results when that occurs. In fact, those that may allocate the credit as we tighten up on it may allocate it quite differently than you and I might do it. Given the inclination lately to abandon housing policies as opposed to supporting one, if you gave additional credit allocation discretionary authority or controls to the existing structure, I'm afraid that there would be more funds drained out of the sector, not funds drained into it.

So I worry about that as a general principle, but surely small business is now under attack because high interest rates give an incentive now for bigness that really does not exist when we get back to normal times. But there will be no chance to go back from bigness to smallness and to competition and to innovation and to job creation once we have gone through this period of time.

Mr. **Marriott**. Mr. Chairman, perhaps we could send some specific questions to Mr. Carlson and have him respond.

Mr. **Carlson**. I would be glad to respond.

Mr. **Nowak**. We'll keep the record open for that purpose and I'd like to now recognize Mr. Byron Dorgan from North Dakota. I think it probably was music to his ears when you were talking about the Federal Reserve change policies.

And Mr. Dorgan, I would yield to you at this time.

Mr. **Dorgan**. Thank you, Mr. Nowak. I'm going to have to go to the floor. We're debating the farm bill today and when you come from North Dakota you better be around when they're talking about farming. But I do appreciate your statement. I think it was an extraordinary statement. We get a lot of good statements before these committees, but I think this one was extraordinarily good.

As I've mentioned before, the first bill that I introduced in Congress was the "Paul Volcker Retirement Act," which was just as a symbol of my disappointment with the Federal Reserve Board. But a couple of points:

No. 1: The $695 billion figure that you used for budget outlays was never a figure that anybody around here used with any seriousness. It was David Stockman's figure based on his estimates of how the economy would perform, which included an 8.9 percent estimated interest rate on 90-day T-bills. Well, most people smiled when they looked at that $695 billion. So when you're using numbers such as $695 billion, understand that no one here in Congress seriously accepted those numbers as being very accurate estimates.

Second, your discussion about free enterprise was very, very good. And I've constrained myself for months talking about this issue because there's a notion that you are first, partisan, and second, anti-business, if you start talking about it.

But I think that the folks who occupy seats in this administration who profess to be such great lovers of free markets and free enterprise are doing as much to undermine the competition in our society and undermine the free enterprise system as any administration I've ever seen.

I don't know that they do it willingly or by intent, but the fact is that the result of the merger mania that we're seeing in this country, including the effect that rising interest rates have on small business versus big business as a consequence of credit hoarding, is to really undermine and threaten the free enterprise system as we know it.

And I really appreciate your speaking out on that. I think it's time that many of us start speaking on that issue.

Finally, I would like to ask you a question. It just seems to me that Wall Street is starting to take a look at the arithmetic and America is starting to take a look, emotionally, at the arithmetic and saying, "If you have the largest tax cut in American history and the largest military buildup in American history, how then can you have a balanced Federal budget?"

And when you ask that question, you come up with the answer: I guess you probably can't. I guess it doesn't all add up somehow.

Isn't that just a terribly conflicting strategy of fiscal policy?

Mr. **Carlson**. Yes, sir. If you asked me to take a wager, I would be willing to bet anybody that we do not achieve a balanced budget in 1984. In fact, I'm hopeful we can keep the deficit below $100 billion by then. The threat is clearly to go up with the budget deficit instead of down.

May I just indicate in the case of Paul Volcker? One always worries about replacements. Not that Beryl Sprinkel, who has talked about being a future chairman, isn't an outstanding individual but I think a monetarist who believes in tighter money growth policies may not be the best thing for the small business community.

So, I'm not so sure replacement of Volcker and picking up a Beryl Sprinkel or somebody who has that philosophical view of the world would be particularly helpful.

On the $695 billion, I think it's important, given the fact the community is so trigger happy and the confidence in all of our institutions, including Government, is somewhat low, that if we do not believe the $695 billion is the appropriate figure we ought to come out with the appropriate figure up front in the First Concurrent Budget Resolution or the President in his announcements and stop fooling the people, because I think it's starting to backfire in terms of people's confidence in our Government.

On the anticompetitive feature, I think also that our policies are antihousing by nature of the high interest rate policy and we're bailing out institutions that cannot survive with these high interest rates, the savings and loans, which is our national housing policy, with no substitute in mind.

We're doing double damage here in the process. And it is important for the Congress to say, "OK. The housing policy we've had for 40 years—we know a better way to take care of the democratic values that exist in housing and all that. We're going to do it a different way, not just to abandon what you have and not have the other in mind."

Mr. **Dorgan**. Mr. Chairman, just one quick comment. You mentioned Mr. Sprinkel and others. In politics, it's a custom for us to speak well of each other generally. That is not necessarily a custom that economists must honor. And I want to say that I share your concern about who the future appointment might be to the new vacancy.

But I just want to conclude with one more quick question. How, in your estimation, can any economist who has been trained beyond 1 or 2 years in college in the field of economics continue to support fiscal policy that is based on expansion and monetary policy that's designed solely to retard growth? That's exactly what we have and yet, we see the spectacle of economists supporting those contradictions and expecting the American people, who know better, to believe that somehow it's going to result in future economic health.

Mr. CARLSON. I agree with you. It's not only anticompetitive, antismall business, antihousing, it's also anticapital formation. And in the future we're going to have fewer labor hours coming into the marketplace, as women are employed just about as fully as men are and the teenagers are a smaller percentage of our population.

The only opportunity we have of improving our standard of living and supporting defense and other things that we wish to buy is through more capital deepening, more capital formation. And high interest rates, of course, are a way to thwart that.

One could make the argument that the reason for the deficit going up is because of tax cuts that help the supply-side economy. But I draw your attention that the proportion of this tax relief that goes for encouraging savings and investment is only around 28 percent, which is the average over the last 20 years of all tax relief measures encouraging savings and investment.

So this isn't necessarily very heavy in terms of encouragement of capital formation. It's primarily encouragement of consumption which has been the experience of other tax relief measures we've had.

Mr. DORGAN. Again, I think your statement was extraordinary and I appreciate it.

Mr. NOWAK. Thank you very much.

Olympia Snowe from Maine.

Mrs. SNOWE. And thank you Dr. Carlson for your very thorough statement. I'll just ask a quick question because I understand you're limited for time.

Could you tell me if there are any correlations—direct correlations—between increases in the prime rate and the number of business failures?

Mr. CARLSON. Yes——

Mrs. SNOWE [continuing]. Especially with the fluctuation of the interest—of the prime rate—from 0.25 percent to 0.50 percent or a point increase?

Mr. CARLSON. Yes, there are, but you have to look at lags. Often a person is in the verge of bankruptcy but before the formal legal declaration occurs, it may be 6 months, 9 months, somewhat later, as people try to work out an accommodation without actually going into bankruptcy.

I did some analysis on that years ago. Yes, there is definitely a relationship. And as the chairman indicated, bankruptcies are going up, and we've had enough for the lag time to take effect, because the downtime has been so long in this case.

I might also say just for humorous indications, we did some analyses to show what the unemployment rate and interest rate effect is on the next election of House of Representatives members. And there's a great deal of sensitivity in terms of increases in interest rates and unemployment rates on the change of the predominant party.

Mrs. SNOWE. We'd like to look at that.

Mr. **Dorgan**. Could you be more specific on this committee, Jack?

Mrs. **Snowe**. One last question. The Federal Reserve Board targets for the growth of money supply. Don't those targets, in fact, suggest an increase in the money supply?

Mr. **Carlson**. Yes; they do and also they consider that each dollar will whip around the economy faster, velocity will be faster.

But to help the economy, while bringing down the inflation rate, they'd have to have a very high assumption—no experience we've ever had yet would justify that—that each dollar would ship around, because the growth rate is so small.

We're not talking about a big change in the growth rate. Just 1 to 2 percentage points faster in the growth rate, we think, will make a significant difference in bringing down long-term interest rates as well as the short-term interest rates. And it's the long-term interest rates that are in the greatest trouble right now, even though short-term rates are also very high.

Mrs. **Snowe**. Thank you. Thank you, Mr. Chairman.

Mr. **Nowak**. Thank you very much, Mr. Carlson. You've put an awful lot of this in proper perspective. And talking about the supply-side premises as a basis for the predictions of the administration, I see that both Wall Street and you agree that there may be some problems ahead. Most of the economists that have run their econometric models also have verified that there has been some tremendous optimism that's not shared by many out there. We're going to have continued problems unless we can pull back, as you've said, either on the one side or the other side, and get some stability out there as fast as we can.

We certainly appreciate your testimony and we'll allow the record to remain open for other members' questions.

Mr. **Nowak**. We got you out 5 minutes later, but you should still be in good shape.

The next witness is from the National Association of Homebuilders, Fred Napolitano.

Mr. **Napolitano**. Mr. Chairman, Jack Carlson is a very difficult act to follow. He is very thorough.

Mr. **Nowak**. He's been at this a long time.

Mr. **Napolitano**. Right. If I may, I will try to condense my statement. May we submit our full report for the record?

Mr. **Nowak**. You certainly may.

Mr. **Napolitano**. I appreciate that.

[Prepared statement of the National Association of Home Builders follows:]

PREPARED STATEMENT OF THE NATIONAL ASSOCIATION OF HOME BUILDERS

Mr. Chairman and members of the committee, my name is Frederick J. Napolitano and I am a homebuilder from Virginia Beach, Virginia. I am testifying today on behalf of the more than 123,000 members of the National Association of Home Builders (NAHB), of which I am President-Elect. Also accompanying me today are Robert D. Bannister, Senior Staff Vice President for Government Affairs and Jim Schuyler, Staff Vice President and Legislative Counsel for Governmental Affairs.

For the past 30 years, I have been active in the construction industry. As President of Napolitano Enterprises I have built more than 6,000 homes and developed more than 5,000 lots. I have also been involved in the development of shopping centers and office parks.

We are deeply appreciative to the Chairman for scheduling these most timely hearings on the devastating impact of high interest rates on small business.

Mr. Chairman, it is traditional for a witness to say how pleased he is to appear before this Committee. But as I think of why I am here and the condition of the economy, the word "pleasure" does not easily come to mind. Words like "deeply troubled" and "impending catastrophe" seem much more appropriate today.

I'm afraid that my message today is similar to our last appearance before this Committee in April of 1980—except that our dire predictions in 1980 have come true. At that time we said "the homebuilding industry is in serious trouble and is on the verge of collapse. If conditions do not change, the homebuilding business, in effect, will be put out of business. This will mean a serious loss of jobs, loss of federal revenue and devastating impact on the homebuilding public." And I don't think that we exaggerated the impact.

OUTLOOK FOR HOUSING

What is the current state of the housing industry? Mr. Chairman, one of the largest and most important industries in America is virtually out of business.

New housing production for August was at a seasonally adjusted annual rate of 937,000—the lowest monthly rate since February 1975.

Housing sales for August fell by 14 percent to 362,000 units, the third lowest figure since the Census Bureau began keeping seasonally adjusted records in 1963.

Our projections indicate that housing production for 1981 may end up at only 1.07 million units—the lowest year since 1946. Unless interest rates decline sharply, 1982 production levels will probably also be at about the one million level.

What about jobs? According to government statistics, 828,000 wage and salary workers in construction are unemployed. Add to this figure about 200,000 more who are self-employed.

The unemployment rate of 16.3 percent (more than double the overall rate of unemployment) will likely increase to 19 percent by the end of the year—and go higher in early 1982.

A mere 2 percent of builders report that sales are "good to excellent." That compares with 70 percent to 80 percent in a good year.

Traffic at subdivisions is almost non-existent—fewer than 7 percent of builders report traffic to be "good to excellent." That compares with 40 percent to 50 percent in a good year.

Failure rate among construction firms is up 41 percent for the period January to August 1981 as compared to the same period in 1980. Failure rate among subcontractors is up by 127 percent.

Mortgage money generally is not available, and what is being offered is at record rates. Freddie Mac yields are over 19 percent in early October.

In short, housing activity has come to a standstill across the country in the face of persistent high interest rates. And our nation's homebuilders are fighting for survival against mounting odds.

ECONOMIC IMPACT

What is the economic impact? From the beginning of the slump in 1978 until today, we estimate that this housing downturn has cost the American economy more than 2.8 million man-years of employment, $49.2 billion in wages and $15.7 billion in total tax revenues. The total overall economic impact has been $223 billion.

The long-term effects will be at least as damaging. The record demand for housing will continue to go unmet, thereby increasing inflationary pressures during the housing recovery. Thousands of skilled craftsmen have sought employment elsewhere and will not return as the housing industry rebounds. Consequently, a new workforce will have to be trained when economic conditions improve.

Building material manufacturers have gone out of business and others have indefinitely delayed any plans to expand production capacity. As in past housing cycles, we will find serious shortages of building materials when production picks up. All of this translates into higher housing prices for housing consumers who are already stretched to the limit of their ability to pay.

Finally, and most significantly for this Committee, I believe that we will see a major shift away from the "small business" character of this industry when the market is revived. Business failures are up by 41 percent over last year, and the smallest and least capitalized firms are the ones which are most likely to go under. The net result will be fewer and larger building firms and a massive influx of foreign capital to purchase developed land and building firms. And, Mr. Chairman, that would be a real tragedy. This industry could lose one of its basic strengths if we lose our base of smaller, fiercely independent and competitive builders.

HOUSING CONSUMERS

What can I say regarding the homebuying and renting public? We have emphasized repeatedly in our appearances before Congress the record demand for housing during this decade. Projections indicate that in the 1980's some 41 million people will reach the prime homebuying age of 30. This compares with about 31 million who reached the age of 30 during the 1970's. The rate of new household formations will be 24 percent higher in the 1980's than during the last decade. All I can add is that if housing production is at about the one million level for the first two years of that decade, we will fall even further behind in meeting that demand. And I believe that unless this demand is met, there will be a revolution at the ballot box in 1982 and 1984.

Let me quote from a letter to the editor of the Business section of the New York Times just a few weeks ago. "If Mr. Average American can no longer own his own home, what does that do to his sense of involvement? Think about it. Lack of mortgage money will tend to destabilize the United States." We share the view that homeownership provides benefits to society far beyond the provision of shelter. These effects are economic, social and political. Obviously, housing production has a substantial direct impact in terms of job creation for construction workers, building material suppliers and the entire network of subcontractors. In addition, there is a significant multiplier effect on the whole range of industries which provide products and services for the home. The social benefits of housing are perhaps less tangible but equally as important. The opportunity for home-ownership promotes stability and a sense of well-being for the American family. Decent housing allows for privacy and the sense of pride that accompanies ownership of property. Finally, the most important aspect of meeting our housing needs may be political. Homeownership and the ability to live in decent and safe housing gives our people the chance to become a part of the capitalist system. Historically, this has led to a strong middle class, which reflects political stability and security. The ability to own a home is still a fundamental part of the American dream and a continuing aspiration for almost all of our people.

But what is today's reality? Unfortunately, the numbers on affordability tell the sad story simply but graphically.

A modest $60,000 mortgage loan at 9 percent interest—the going rate two years ago—required a monthly payment of $483. At 16½ percent, the payment is $831 per month, almost double the payment of two years ago. In order to meet those monthly payments, a family would need an annual income of almost $40,000. Only 19.5 percent of the American people have an income high enough to afford that home, and virtually no first-time homebuyers would qualify for a home at those interest rates.

UNLOCK THE ECONOMY PROGRAM

In order to focus national attention on the impact of high interest rates on credit sensitive industries, we recently began an "Unlock the Economy" campaign which was developed at our NAHB Board of Directors meeting in September. We joined in a coalition with the National Association of Realtors and the National Automobile Dealers Association. There are three basic elements to this program to combat high interest rates:

First, we call upon the Administration and Congress to meet the initial Administration targets of less than $42.5 billion deficit in fiscal year 1982 and a balanced budget in fiscal year 1984. We recognize that this will require substantial reductions in defense expenditures and additional cuts in non-defense expenditures as well as reductions in entitlement programs. It may even involve deferral of the individual income tax reductions already approved by Congress.

Second, we then call upon the Federal Reserve Board to institute policies that will allow the money supply to grow at the upper end of the ranges of the Fed monetary targets and at a rate that will accommodate economic growth and stability. In this effort, we seek the support of the President and Congress for this change in Fed policy.

Third, we seek to broaden the representation on the Fed. Board of Governors to include representatives from the credit-sensitive small business sector of the economy. We would support the appointment of a small business person to the Fed when the term of Vice Chairman Schultz ends early next year.

On October 6, hundreds of the nation's homebuilders were in Washington to ask Congress for immediate action to bring interest rates down. On October 9, local and state homebuilder associations across the country, in conjunction with the Realtors and the Auto Dealers, staged rallies to "Unlock the Economy". The keys that are being sent to Members of Congress are a symbol of the plight of small businessmen and women and that the key to unlocking the economy is lower interest rates.

Regarding budget reductions, Mr. Chairman, federal housing programs have already borne a large percentage of the cuts. We believe that further budget cuts should be concentrated in areas which have been relatively untouched, such as defense programs. In addition, we strongly support revision of the Consumer Price Index to more accurately reflect housing costs. This revision would affect most entitlement programs. However, because of the urgent need to reduce interest rates, we would not oppose further cuts in direct expenditures for housing programs if necessary.

But I want to make it clear that we would strongly oppose "cuts" in the ceiling for the unsubsidized FHA insurance programs and the Government National Mortgage Association (GNMA) mortgage-backed securities program. Mr. Chairman, in 1980 GNMA purchased over 73 percent of the FHA-insured non-subsidized mortgages and, as significantly, over 72 percent of the VA-guaranteed loans.

We have not yet been informed of the magnitude of "cuts" in commitments for the GNMA program proposed by the Administration or whether any cuts in FHA commitments have been proposed. But reducing the level of FHA activity and VA activity (through the backdoor of reducing GNMA purchases) could have a severe impact on the housing industry. And it could not occur at a worse time. Deregulation of financial institutions will, by its very nature, force the mortgage market into greater reliance on general capital markets and make the secondary markets (GNMA, FNMA and Freddie Mac) more significant. In a depressed market, VA and FHA guaranteed or insured mortgages accounted for 300,000 or 22 percent of total housing starts in 1980. As you are aware, FHA and VA represent the only significant source of fixed-rate long-term mortgage available, and any restriction in their capacity to operate as demand programs would severely impact potential first-time buyers and veterans who are otherwise not served or priced out of the market.

Mr. Chairman, there continues to be a vital role for FHA and VA unsubsidized programs today. They are extremely important in a tight housing market because they always offer lower downpayments and generally provide homeownership for families who would otherwise not qualify for conventional loans. FHA remains the lender of last resort providing mortgage credit when conventional lenders have fled the market. The VA program remains an entitlement for servicemen who have ably served our country. Finally, these programs not only do not cost the government money—they produce a net surplus to the Treasury with a minimum of defaults.

Regarding Federal Reserve Board policy, I was pleased to read Treasury Secretary Regan's recent statement where he indicated the need for the Fed to gradually ease its monetary policy in order to "enable the economy to recover nicely from its current flat period." This latest statement by the Treasury Secretary represents some recognition that overreliance on monetary policy can be counterproductive.

Regarding other issues which specifically affect housing, we believe that there are a number of actions which could have a positive short-term and long-term impact.

First, we strongly believe that immediate action must be taken to make the tax-exempt housing bond program workable through passage of technical correction legislation sponsored by Representative John Duncan (R-TN) as H.R. 3614 and in the Senate by Senator Sasser (D-TN) and Senator Baker (R-TN) as S. 1348. In addition, the Treasury Department should redraft and simplify the complex and unworkable regulations issued for the single-family program. The Treasury Department should also act expeditiously to issue the regulations implementing the multifamily program, which may well become the major production vehicle for low and moderate income families.

Second, we strongly support legislation recently introduced by Representative Volkmer (D-MO) as H.R. 3704 and in the Senate by Senator Hatch (R-UT) as S. 1678. This bill would encourage increased pension investment in residential mortgages by eliminating the so-called "prohibited transaction" provision in the ERISA law and by recognizing investment in residential mortgages as a "prudent investment."

Mr. Chairman, pension funds represent the single largest pool of long-term investment capital with assets of $600 billion. Public and private pension funds are expected to reach a level of $1.3 trillion by 1985. We believe that the artificial legislative barriers to investment in residential mortgages should be eliminated and that Congress should put its stamp of approval on prudent and safe investments in housing.

Third, we believe that there should be increased Congressional oversight of Federal Reserve Board activities, and we would support legislation to shorten the term of Fed members.

Fourth, we believe that the Credit Control Act, which is due to expire on June 30, 1982, should be reauthorized and consideration given to specifying conditions for its activation and direction given as to which powers should be exercised in order to more fairly share the credit burden throughout the country.

Mr. Chairman, I cannot in good conscience say that enactment of this program would lead to a healthy economy and a robust housing industry in the next three to six months. And because of the imminent danger of bankruptcy to many builders over that period of time, I am not optimistic about the short-term outlook. But such a program would give a signal—to the Fed, to Wall Street, to the housing consumer and the homebuilder—that we have begun to turn a corner and that if we can just hang on a little longer, then economic conditions will improve.

As I assume the leadership of NAHB in January, I would like to be able to give our members—and the homebuying and renting public—that message. Mr. Chairman, I hope that we can continue to work together to achieve that goal.

TESTIMONY OF FREDERICK J. NAPOLITANO, PRESIDENT-ELECT, NATIONAL ASSOCIATION OF HOME BUILDERS, ACCOMPANIED BY ROBERT D BANNISTER, SENIOR STAFF VICE PRESIDENT FOR GOVERNMENT AFFAIRS, AND JIM SCHUYLER, STAFF VICE PRESIDENT AND LEGISLATIVE COUNSEL FOR GOVERNMENT AFFAIRS

Mr. NAPOLITANO. As you pointed out, my name is Frederick J. Napolitano. I am a homebuilder from Virginia Beach, Va. I am testifying today on behalf of the 123,000 members of the National Association of Home Builders, of which I am president-elect. Also accompanying me today are Robert D Bannister, senior staff vice president for government affairs and Jim Schuyler, staff vice president and legislative counsel for government affairs.

For the past 30 years, I have been active in the construction industry, and as president of Napolitano Enterprises I have built more than 6,000 homes and developed more than 5,000 lots. I have also been involved in the development of small shopping centers and office parks.

The reason I say that is because I am involved very deeply in small business, in many facets of it and I know the problems that have existed over the years, and especially those that exist today in the economic climate that we have.

We appreciate very much the fact that the chairman has called this meeting to talk about the devastating impact of high interest rates on small business.

Pardon me. Let me just for a moment digress. I'm sure that most of you have seen in the morning paper, the Washington Post, an article entitled "Patience Counseled on Housing." And this was yesterday. Jerry Jordan, who is a member of the President's Council of Economic Advisers, testifying before Chairman St Germain's committee, said that the homebuilding industry and people who own housing should be very patient. I might point out to you that the homebuilding industry has been patient for the last 2 years, since 1979 when this tight money policy began, and we're at the point of having no patience left.

He also points out in here, which was very amusing, that he claims next year that we should show a level of 1.8 million units while demand is projected to be 2.5 million units. Well, I'd be willing this morning to settle for even 1.7 if he would guarantee that.

And you wouldn't see us in the Halls of Congress or in the administration for the next year or so if he can guarantee those figures.

Unfortunately, our figures for this year look like they probably will be just under the 1 million range, and our projection, based on today's scenario, for next year is about 1.29 million units, which is not very good. It's a little bit of an increase but obviously not good when you consider the fact that in a good year—1978 being the last good year—we built 2 million units. And when the demographers do show that we need probably 2 to 2.5 million units a year you can see how much further behind we're getting in housing the American people.

I'm afraid that my message today is similar to our last appearance before this committee in April of 1980 except that our dire predictions in 1980, unfortunately, have come true. At that time we said, "the homebuilding industry is in serious trouble and on the verge of collapse. If conditions do not change, the homebuilding business, in effect, will be put out of business. This will mean a serious loss of jobs, loss of Federal revenue, and a devastating impact on the home-buying public." And I don't think we exaggerated the impact.

That impact is that from the beginning of the slump in 1978 until today, we estimate that this housing downturn has cost the American economy more than 2.8 million man-years of employment, $49.2 billion in wages, and $15.7 billion in total tax revenues. The total overall economic impact has been $223 billion.

The long-term effects will be at least as damaging. The record demand for housing will continue to go unmet, thereby increasing inflationary pressures during the housing recovery. Thousands of skilled craftsmen have sought employment elsewhere and will not return as the housing industry begins to rebound.

Finally, and most significant to this committee, I believe that we will see a major shift away from the small business character of this industry when the market is revived.

Business failures—someone asked about this before—are up 41 percent over last year, and the smallest and least capitalized firms are the ones which are likely to go under first. The net result will be fewer and larger building firms and a massive influx of foreign capital to purchase developed land and building firms.

It's unfortunate that we've come to that stage where the small business person in this country, and especially the builder, will no longer be a competitive force in this country.

What can I say regarding the homebuying and the renting public? Well, we've emphasized repeatedly in our appearances before Congress the record demand for housing, as I mentioned earlier, in this decade.

Records indicate that in the 1980's 41 million people will reach the prime homebuying age of 30 as compared to about 31 million during the 1970's. And the rate of new household formations will be 25 percent higher in the 1980's than during the last decade.

All I can add is that if housing production is at about the 1 million level, as I said for this year, then for the first 2 years of the decade we will fall even further behind in meeting that demand.

A modest $60,000 mortgage loan at 9 percent, which was not too long ago the going rate, required a monthly payment of $483. At

16½ percent, which is even on the low side today, the payment is $831 per month, or almost double the payment of 2 years ago.

In order to meet these monthly payments, a family would need an annual income of almost $40,000. And only 19.5 percent of the American people have an income high enough to afford that home. And virtually no first-time homebuyers would qualify for a home at those high interest rates.

In order to focus national attention on the impact of high interest rates on credit sensitive industries, we recently began what we call an "Unlock the Economy" campaign, which was developed at our NAHB board of directors meeting in September. We joined in a coalition with the National Association of Realtors and the National Automobile Dealers Association.

There are three basic elements to this program to combat high interest rates. First we call upon the administration and the Congress, as Mr. Carlson mentioned earlier, to meet the initial administration targets of less than $42.5 billion deficit in fiscal year 1982. We had a discussion on that, so I won't prolong that.

Second, we call upon the Federal Reserve Board again to institute policies that will allow the money supply to grow at the upper end of the ranges of the Fed monetary targets and at a rate that will accommodate economic growth and stability.

Third, we ask that for the Federal Reserve Board of Governors, the next representative named be someone from the credit-sensitive small business community.

Now, regarding budget reductions, Mr. Chairman, the Federal housing programs have already borne a large percentage of the cuts—in fact, an unfair percentage of the total cuts that have taken place. We believe that further budget cuts should be concentrated in areas which have been relatively untouched, such as the defense programs.

In addition, we strongly support the revision of the Consumer Price Index to more accurately reflect the housing costs. This revision would affect most entitlement programs. However, because of the urgent need to reduce interest rates, we would not oppose further cuts in our industry as long as those cuts are equal and across-the-board and everybody is taking their fair share of cuts.

But I want to make it clear that we would strongly oppose cuts in the ceiling for the unsubsidized FHA insurance programs and the Government National Mortgage Association—known as GNMA—mortgage-backed securities programs.

Mr. Chairman, in 1980, the GNMA purchased over 73 percent of the FHA-insured nonsubsidized mortgages and, as significantly, over 72 percent of the VA guaranteed loans.

Deregulation of financial institutions will, by its very nature, force the mortgage market into greater reliance on general capital markets and make the secondary markets—GNMA, FNMA, and Freddie Mac—much more significant.

In a depressed market, the VA and the FHA guaranteed or insured mortgages accounted for 300,000 units or 22 percent of total housing starts in 1980.

As you are aware, the FHA and VA represent the only significant source of fixed-rate long-term mortgage available and any restrictions in their capacity to operate as demand programs would severely impact potential first-time buyers and veterans who are not otherwise served and would be priced out of the marketplace.

Regarding other issues which specifically affect housing, we believe that there are a number of actions which could have a positive short- and long-term impact.

Without going into a lot of detail, one of them is the tax-exempt housing bond program which was passed by the Congress to be in effect for another 2 years. We're asking that you support H.R. 3614, which would make technical corrections to the legislation. The administration, unfortunately, and the Treasury Department, are dragging their feet. Treasury should redraft and simplify the complex and unworkable regulations issued for the single family program. Treasury should also release regulations to implement the multifamily program. There are some problems so that we cannot use the law as it was passed originally. We ask that you would support passage of technical correction legislation.

Also in the Senate, there's the Senate bill, S. 1348.

Second, we strongly support legislation recently introduced by Representative Volkmer, known as H.R. 3704 and by Senator Hatch, known as S. 1678. This bill would encourage increased pension investments in residential mortgages by eliminating the so-called prohibited transaction provision in the ERISA law. We understand that the Secretary of Labor can do this internally if he so desires. He has been unwilling to do anything so far. Therefore, we need to have the Congress do something about it.

Third, we believe that there should be increased congressional oversight of the Federal Reserve Board activities and we would support legislation to shorten the term of the Fed members so that perhaps there could be some turnover, especially in times like this.

Fourth, we believe that the Credit Control Act, which is due to expire on June 30, 1982, should be reauthorized and consideration given to specifying conditions for its activation and direction given as to which powers should be exercised in order to more fairly share the credit burden throughout this country.

Mr. Chairman, I cannot in good conscience say that the enactment of this program would lead to a healthy economy and that a robust housing industry would come back in the next 3 to 6 months. And because of the imminent danger of bankruptcy of many builders over that period of time, I am very much concerned that all we're doing now is putting some bandaids on it in order to have these people survive. I am not optimistic about the short-term outlook.

But such a program would give a signal to the Fed, to Wall Street, to the housing consumer, and to the homebuilder that we have begun to turn a corner and if we just hang in there a little longer, the economic conditions will improve.

As I assume the leadership in January of this association, I would like to be able to give that message to our members. Mr. Chairman, I will conclude at that point. I have many horror stories that I can give you. And if you would care to go into that, I would be happy to discuss with you what is happening on almost an area-by-area basis with our industry.

Thank you.

Mr. Nowak. Well, thank you very much.

Let me just ask a couple of questions here. From the unwillingness of the administration to move in this interest rate area to some degree or to look at a solution to this problem, at least in this member's mind, it becomes very evident that the administration no longer considers housing as an investment. And you know, it's one of the unknown factors here, people sit silently by until they're ready to sell or have to sell or, on the other hand, have to buy on a move, and then they're faced with the realities of what this interest rate situation is all about.

By the same token, those who have purchased with the hopes of building equity in a home, over the last year and a half at least, have found that they're not keeping up with inflation. The home as an investment has probably not kept up with the inflation rate over the last year. In general, has that seemed to be a national trend, and do you estimate the kind of appreciation that has taken place as this interest rate has gone up, and what is the relationship of people's growth in appreciation over this period of time?

Mr. **Napolitano**. Well, there are many things that are happening out there. As our builders face bankruptcy, they are stuck with inventory homes that they must move. They begin to lower the price of those homes. They do what we call buy down the interest rate. They do anything they can at this time to move the inventory. Well, this results in prices coming down in some areas and it would vary from area to area depending on what the inventory rate is.

Well, obviously if the new homes are going for less, the existing homes start to move for less money also. So the people are not getting the return that they thought they were getting out of their homes.

I don't think it's something that is happening throughout the country. It may be spotty. I don't think it's a trend that we're seeing that will continue if the interest rate starts to come down, if homebuilding begins to pick up again.

I believe that there is pent-up demand because of the 41 million Americans who will be in the marketplace and are waiting to buy a home today. I believe as we get back into building—and this is one of the unfortunate situations—as we get back to building we will find that we have to get labor back into the homebuilding industry, we will have to get our sawmills moving again. We're going to find that tremendous shortages have been created—shortages of labor, shortages of material. Prices will begin to move up again and I think then you'll see that those homes will be worth a lot more than they are at the present time. I think you'll see a normal growth rate at that stage.

Mr. **Nowak**. Mr. Marriott?

Mr. **Marriott**. Thank you, Mr. Chairman. I would like to congratulate you on an excellent statement. I've met with the homebuilders in my district many times and I'm well aware of the tremendous problems.

It seems to me that we can talk about the credit control and tax-exempt housing bonds and the Federal Reserve Board and all the rest; but, your business is at the mercy of interest rates—the solution is get the interest rates down. You're in sort of a boom or bust business, but the bust has been 10 times greater than in normal periods.

Do you have any suggestions on immediate ways of getting the interest rate down? As I was talking to Mr. Carlson, it seems to me that the policy of supply-side economics is going to keep the interest rates up a while, until we see if these tax cuts really do stimulate the economy.

Now, are we strictly in a waiting game here or do you see anything on the horizon to really bring those rates down in a hurry?

Mr. NAPOLITANO. I see a catch-22 situation. The best thing that could get homebuilding moving again would be a drop in the interest rates tomorrow down to 10, 11, 12 percent.

Mr. MARRIOTT. Absolutely.

Mr. NAPOLITANO. But unfortunately, we firmly also believe that this would be disastrous to us in the long run. The long run could be 3 months, 6 months down the road. This happened to us last year during the summer. Our people especially are very optimistic by nature—we have to be to be in the type of business we are. We're providing shelter for the American people. We'll go out there and buy the lots and start building the homes and then the rate changes on us again and then we're stuck with more inventory.

So we don't want to see that happen. We are not advocating that there be a tremendous drop very quickly. We would rather see a slow, sustained drop, and what we're saying today with the prime rate coming down from 20 to 18, this is fine, it's a good indication, if it continues along those lines. But I read in the paper where the economists are already talking that this may be the bottom again. It may start to move up at this stage.

We can't conduct business in those conditions. It changes daily, as Mr. Carlson mentioned before.

No, I don't see anything. In talking with Mr. Volcker in meetings that I have had with him and other people from the Federal Reserve and other people on Wall Street—they all say the same thing. I don't know if they're right or not, but they all say the same thing—that unless the budget is brought in line, you will not see the rates come down. So, if that is the true answer to it, then that's what we should be doing. That's the only solution we see at this moment.

Mr. MARRIOTT. But it's not a short-term solution. That's the problem. It takes time.

There are a number of small businesses and large businesses who get "Government cost of money" loans. Do you think it will ever come to the point where the homebuilding people are going to be in here looking for Government sources of money at Government interest rates?

Mr. NAPOLITANO. The homebuilding industry has been getting away from subsidies. We believe in the free marketplace and we respect that and we want to see that happen. If we continue along the lines we're going with the high interest rates, more bankruptcies, and our homebuilders having no other way of competing—the homebuying public cannot compete with the General Motors and the big companies in this country, with the conglomerates—then I could see us possibly coming in here and saying, "We must have some relief to house the American people."

Mr. **Marriott**. Very quickly. Do I understand you lost about 40 percent of the homebuilders in the last year?

Mr. **Napolitano**. No; the bankruptcy rates were 41 percent above last year which means they're continually increasing.

Mr. **Marriott**. And if the interest rates stay where they are for the next year, what additional losses do you expect?

Mr. **Napolitano**. I would see another 40 to 50, without any question about it. Many of our people are just hanging in there right now. They can't last 60 to 90 days.

Mr. **Marriott**. Thank you very much.

Mr. **Nowak**. Just a short question also. If we conclude in this country that we'll run housing without the FHA or any of the other mortgage subsidy programs, and we no longer look at housing then as an investment for equity growth for an individual, won't there be a tremendous shift from private ownership in either condominiums or single-family homes? And won't you force an awful lot of people into a renter's situation? Because of the increase in some of the depreciation schedules, I would assume you're looking at a tremendous growth then in the apartment rental area, which has been dormant for the last 5 or 6 years.

Mr. **Napolitano**. Well, I haven't seen too much growth—it is too early to see the growth yet—or any discussion about the depreciation schedule. I think it will help. I think we'll see some results of that eventually.

Mr. **Nowak**. But wouldn't you think there would be a shift into tremendous rental situations where——

Mr. **Napolitano**. People have to live someplace.

Mr. **Nowak** [continuing]. People won't have any equity building for them for the rest of their lives?

Mr. **Napolitano**. That's right. People will have to be living somewhere.

Mr. **Nowak**. OK. We'll have to take a break. We have a vote on the floor and we have about 9 minutes, gentlemen, to get there.

So, we'll come back and we'll panel some witnesses.

Thank you very much. We'll stand in recess for 10 minutes.

[Brief recess.]

Mr. **Nowak**. The subcommittee will come to order and we'll have two more witnesses come to the table. We have at this time Robert Stoner, who is president of Winfield Industries, a manufacturing firm located in Buffalo, N.Y., and Mr. Stoner, if you'll come forward, and also Mr. Joseph Cobb, who's director of economic analysis for the Council for a Competitive Economy. Mr. Stoner, if you would like to present your testimony and then I think we'll hear from Mr. Cobb and then open up the panel to questions from the members here.

Mr. Stoner.

TESTIMONY OF ROBERT STONER, PRESIDENT, WINFIELD INDUSTRIES, ACCOMPANIED BY JOE COBB, DIRECTOR OF ECONOMIC ANALYSIS, COUNCIL FOR A COMPETITIVE ECONOMY

Mr. STONER. Thank you, Mr. Chairman, and distinguished members of this House Small Business Subcommittee for this opportunity to testify before you on the effect of high interest rates on small business in the Buffalo, N.Y., area.

As stated, I am Robert Stoner, president of Winfield Industries, a small manufacturing firm located in the city of Buffalo. I am also on the board of directors and vice chairman of C.O.S.B.E., the Council of Small Business Enterprises, a part of the Buffalo Chamber of Commerce. I would like to state, however, that this testimony which I am about to give is my own and does not necessarily represent the position of C.O.S.B.E.

I think it's also interesting to note that almost 2 years ago I was here to testify on this same subject and, although a lot of events have transpired and the prime has moved from 14½ percent, which it was then, up to about, I guess, 18 which it is now, I don't see dramatically different results on small business caused by interest rates.

As one who is active in small business affairs and as the owner and manager of my own small business, I have the opportunity to speak with many small business persons in our area. As such, I might be expected to speak for small business and, indeed, this I will try to do. Because of the diversity of small business, however, retailers, service organizations, manufacturers, contractors, wholesalers, all serving a variety of markets, new businesses and old, 2 to 200 persons, individual proprietorships, partnerships and corporations, it is always, I think, very dangerous to generalize about any factor affecting business, and high interest rates are no exception.

In spite of this, we all know the importance of interest rates on small business. The only significant source of funds outside of the entrepreneur's equity capital and his retained earnings are his borrowed funds. As such, the cost of these funds can be a major cost in doing business and a cost over which he has little control once the commitment to borrowed funds has been made.

In preparing this testimony, I contacted a number of my fellow small business operators and received from them the following comments, such as, a small manufacturer said:

> It's great. Business has slowed. I've laid off a few people, but the result of the slower business has been my receivables and a portion of my inventory has been turned into cash which I have invested at 16 to 17 percent interest.

Another small and obviously successful manufacturer said:

> I have an established, unsecured line of credit at Marine Midland Bank for $200,000 at prime. Other banks are knocking on my door offering funds at similar terms.

An industrial distributor:

> I am modestly levered but can handle the costs at the expense of profits. I'm stopped cold, however, in plans to expand branch operations and the addition of new product lines which would require more borrowed funds. The high cost of these funds compared to the expected rate of return does not justify the risk.

Another industrial distributor:

> I opened a branch in Rochester a few years ago with 9 percent money. The branch turns a modest operating profit, but with these same funds now costing 21 percent, the operating profit is a net loss. I'm considering closing the branch with a loss of five jobs.

A school supply distributor:

> Today's high interest rates are a significant but not burdensome drain on profits. If we were in our startup position of a few years back when we were heavily levered, however, it would have been a severe problem.

A chairman of a retail organization and president of his own retailing company:

> High interest rates are an increasing cost of doing business and most successful retailers are handling it like all other cost-related problems. Unprofitable product lines, departments or branches, are being cut back or eliminated.

The major problem of retailers as viewed by this man can be much more related to poor management unable to cope with the many changing conditions that constantly impact upon the businessman, rather than a single issue like high interest.

A machine tool distributor:

> The first effect of high interest has been to force me to cut my inventory of new and used machine tools from $1 million down to $200,000. This reduction has reduced my ability to serve my customers as fast as before. Secondly, I now have to be tougher on customers about payment terms. Where formerly I could extend some credit, now I must demand immediate payment.

This distributor finds credit is severely limited to a number of his small machine shop customers, preventing them from purchasing new and more productive equipment, and he is concerned that many of these small shops, unable to upgrade their equipment, may be forced to close.

He estimated that the net result on his business has been a reduction to half that business which he formerly did with small machine shops. He himself, however, has countered this by increasing sales of larger, more sophisticated equipment to larger, more credit-worthy customers. The overall effect on his company, therefore, is not a real problem.

Although this same person served on the local development corporation who has, through favorable interest rates, been able to save businesses and jobs in the city of Buffalo, he would rather see a free market exist without Government interference in interest rates, rather than to give preferential interest loans to selected companies.

A retail card and gift shop owner:

> Fortunately, I have no borrowed funds and therefore, I'm enjoying high interest income on funds not committed to business. I would not, however, consider expanding my business today at these interest rates if borrowed money was required. The returns in my business do not justify it.

Finally, my own firm, a small manufacturer: Our major customers are capital goods manufacturers and they are currently severely depressed, in part, I'm sure, by the high interest that their customers must pay. My business volume, therefore, is off about 35 percent compared to last year, with a loss of about 35 jobs. Profits have been disproportionately reduced to an even greater extent. Fortunately, however, receivables and inventory reductions have been converted to cash and this is invested at favorable money market rates. This year, approximately $250,000 in plant and equipment improvement is being financed with retained earnings from previous, more profitable years, and hopefully, when the economy does firm, we can come out of this stronger than we went into it.

It is maybe unfortunate that my view of the effect of high interest rates is through my contacts with principals of well established and well managed small businesses. I have yet to have a personal acquaintance of mine who is the manager of a small business and have him go under. I am well aware that you are receiving testimony, as I heard this morning, from particularly hard-hit segments of our economy such as automotive and construction. You are hearing a dramatically different story.

It is well to note, however, that the group that I did talk to, in the face of today's stagnant economy, is not talking about expansion or the creation of new jobs. I believe that most of them would be unable to justify expansion with borrowed funds at today's rates, considering their normal rates of return and with the high risk of today's economy.

It is perhaps in character with the nature of successful and established small business persons that they are almost unanimous in their opinion that the Government should not try to rig interest rates artificially low for particular companies, industries, or regions. They feel low interest rates given by a Government agency to spur development in one locale or another probably serves little economic purpose in the overall sense.

At the least, preferential interest rates probably distort competitive relationships between regions or companies which existed before one party received the favorable treatment. My peers suggest that the best thing that Government can do is to balance the budget, take the pressure off inflation, and let interest rates take care of themselves.

This is obviously going to cause a lot of hardship to small business. There will be many failures and maybe I'll be one of them, but isn't this the nature of the competitive system that has served our economy so well over the past 200 years? To serve best, the right to fail must equal the right to succeed.

The high interest problem has now been with us for over 2 years and although many have been hurt, many well managed small businesses are profitably growing. What we feel is needed is a freer economy with less Government interference. We need an economy that can grow without ruinous inflation. The small businessman's main problem is the stagnant economy and inflation, not high interest rates. With an expanding economy, with controlled inflation, small businesses will do what they've always been best at doing, in developing new ideas and bringing them to the marketplace. This, in turn, creates the jobs that are so badly needed.

Mr. Chairman and subcommittee members, I wish to thank you for this opportunity to testify and wish you wisdom and success in dealing with these crucial problems.

Mr. NOWAK. Thank you very much, Mr. Stoner, and we'll hold the questions until we have Mr. Cobb's testimony.

Mr. COBB. Thank you, Mr. Chairman. I have a fairly long statement which you can just print in the record and I'll touch very lightly on some of the key points that I want to make.

Mr. Nowak. Without objection, it'll be so ordered.

[Mr. Cobb's prepared statement with attachments follow:]

Prepared Statement of Joe Cobb, Director of Economic Analysis, Council for a Competitive Economy

Mr. Chairman and Members of the Subcommittee. Thank you for this opportunity to testify today about the impact of high interest rates on small business capital formation.

The Council for a Competitive Economy is a national membership organization of business and individuals dedicated to a free, competitive market economy unhampered by regulations, taxation, protectionism, subsidies, or special privileges for any business or labor organization. I am speaking today on behalf of our 1,500 members in all 50 states. Most of our members are owners of small businesses, or individuals working in middle management of larger companies who would like someday to be self employed as proprietors of small businesses.

Of course, every small business is striving to become more successful—the large business firms of today were once small themselves, but they were successful competitors in the free market. This is what the Council for a Competitive Economy stands for: the right of those who satisfy the demands of consumers to grow and prosper, and the necessity of those who do not satisfy the demands of consumers to close up shop—not to come begging to Washington for protection or subsidies or loan guarantees.

The immediate problem in our economy is the cost of capital. This problem affects both large and small businesses, but the impact on small business has several additional dimensions that particularly concern this Subcommittee. In the first place, you know that small business accounts for over 55 percent of all non-agricultural employment and 45 percent of GNP in the United States. It produces over 50 percent of all new inventions, innovations, and patents. In the last ten years, 69 percent of all new jobs were created by firms with less than 100 employees, many located in the centers of large cities. In absolute numbers, there are far more business entities affected by today's high interest rates on the small-business end of the scale than on the larger-business end of the scale.

THE ROLE OF LENDING INSTITUTIONS

In his classic work on banking, Lombard Street (1873), Walter Bagehot, the publisher of The Economist in London, described how the institutions of banking arose. The British economy in those days was so much more advanced in its financial institutions than the rest of Europe and America that his analysis of depository and lending institutions is still the most incisive explanation of how a modern society mobilizes the savings of its economic system and creates capital investment.

In the more primitive societies, Bagehot explained, the people who are able to save a little of their earnings will tend to keep them at home, under the mattress, or buried in the backyard. This kind of saving for a rainy day is satisfactory to the individual, because the money will be securely hidden and will be readily available whenever needed. By 1873 in England, however, the growth of depository and lending institutions had made it possible for people to keep their savings securely on deposit, and for businesses to borrow the funds to finance more complicated modes of production and distribution. This development in England, as well as the U.K.'s policy of international free trade, carried that nation to the top of the world economy. After the Civil War, the United States also developed a nationwide system of depository and lending institutions that carried us to even higher levels of economic development.

What does an institutional lender do that is so important? In the first place, of course, it promises to return the savers' funds either upon demand, or with only a very short delay. This persuades the saver to bring the resources out of the mattress or out of the backyard vault and put them in the hands of the banker. (I will use the term "banker" to refer to all kinds of institutional lenders—including in today's market, thrift institutions, credit unions, money market funds, and insurance companies.) In the second place, the banker gathers information about potential borrowers. It is his skill in making as few bad loans as possible that will bring the banker success; and if his judgment is poor, failure.

Before the development of banking, there were people who made loans with their own money—and sometimes with other people's money too—but every transaction was tailor-made, or negotiated directly on terms ranging from Shylock's "pound of flesh" in the Merchant of Venice to loans without interest, as mandated by the laws of the Church. The development of banking was, in many ways, just like the development of Mr. Woolworth's department stores: there was a posted price for savings—the interest the bank would pay—and a posted price for loans, provided the borrower met the banks' minimum test for credit-worthiness: a job for bankclerks.

What is happening today in the United States, and for that matter all over the world, is that we are regressing. This is the central point I want to make in today's testimony: the efficiency of our capital markets is being destroyed. The first victims of this wholesale destruction are the small businessmen, whose basic position in our society you Congressmen are here to defend. Yet, the process of destruction of our capital markets will not end with the small businessmen: when the capital markets have been destroyed for the small or marginal producer, they will continue to disintegrate for all producers. In the last analysis, a free society will become impossible, because you can't have a capitalist society without long-term capital markets. The capital markets are the only way a free market can plan for the future.

GOVERNMENT REGULATION IS THE PROBLEM

I have published an analysis in The Journal of Retail Banking (which is submitted for the printed record) describing the changes I see coming in the financial services industry. Unless certain important legislative changes are made—and made very soon—in the United States, the problems of inflation, high interest rates, and declining productivity will persist. I support for the record, the legislation introduced in the United States Senate by Banking Committee Chairman Jake Garn, but I do not feel that his proposals go far enough. Nothing short of total deregulation of our capital markets, the financial services industry, and our currency system will solve this fundamental problem of regression and degradation in our capital markets.

I want to turn the balance of my time to the discussion of three questions that relate to your concern about the impact of high interest rates on small business capital formation:

(1) Why are interest rates higher today than ever before in the United States?

(2) Why are interest rates higher for small business than for large business?

(3) Why must the solution be found in more rapid deregulation and not new regulations?

I believe that my analysis of these three questions will also show you why most professional economists who may appear before these various Congressional committees that are seeking answers to the current economic problems are so often at a loss to give you any answers, or why they predict interest rates will come down soon—and then return a few months later with no answer to explain why they were wrong.

WHY INTEREST RATES ARE SKY-HIGH

An interest rate is often described as "the price of money." If you want someone to lend you a dollar, you have to be prepared to pay a few cents for the use of the dollar. The concept is more like renting something than like buying it outright, because at the end of the term of the loan, you have to return the principal. Some people have said that "money is tight," and therefore since available funds are scarce the eager borrowers, who may feel that they have no alternatives, will bid up the price. This explanation ignores the fact that money today is not tight, and that borrowers are not so eager that they are not finding substitutes—including slower business activity.

The "tight money" theory overlooks that fact that money is a special kind of thing that you might want to acquire. Its main difference is that it is the thing that you use, not for its own sake, but for the purpose of obtaining other things. Moreover, it is the only thing that has its price quoted in terms of itself. This last is what makes finance so confusing to most people. If you go to the store and buy a can of beans, the price might be one dollar; but if you want to buy a dollar for a year, the price will be quoted in terms of dollars. The lender today is most interested in something quite different than the scarcity of dollars in the marketplace: he wants to know how many real goods and services the same amount of dollars that he may lend you today will be able to buy in the future.

Why should anybody lend money? Why should anybody give up the real goods and services that the money might buy today—especially if there is a genuine fear, by the lender, that what he gets back in the future won't buy as much? An interest rate of 20 percent is just another way of saying that a lender will agree to give you command of his share of real goods and services today if you will double the amount of dollars in three years. An interest rate of 10 percent implies that the amount of dollars will double in seven years. An interest rate of 7 percent implies that the amount of dollars will double in ten years.

Unfortunately, in this age of inflation, the word "dollar" has no meaning. It has a pronunciation; it has a spelling; it even has a connotation; but it has no meaning for any time-period longer than about ten minutes. Therefore, in today's capital markets lenders are willing to enter into contracts with borrowers (in terms of "dollars") only for shorter and shorter time-periods and then only if they can be assured that the number of dollars will at least double in three years. Because the very word that we use to quote prices has no meaning, lenders and borrowers are forced to become speculators. The borrowers hope that they will be able to put the money to productive use and generate at least enough dollars to pay the high rates, and the lenders are charging the highest possible rates because they worry that they won't get back as much as they lent in the first place. The least honorable speculators, moreover, are those who celebrate the fact that they will be able to pay off their loans in "cheaper dollars"—and it is the growing popularity of that slogan that has made the lenders increasingly aware that they have to charge rates as high as 20 percent just to keep from being ripped off.

The fact that money is not tight, but quite loose, is just more evidence that the lenders must ask for more and more interest just to keep themselves from losing—in terms of real goods and services. The President and the Secretary of the Treasury have paid too much attention to Federal Reserve Board statistics about the money supply, in particular M1-B. These statistics are very misleading, because each narrowly defined monetary aggregate does not take account of nearly perfect substitutes in the money market. The fact alone that M1-B is near the bottom of its target range but M2 is near the top of its target range tells you that something is wrong with the definitions of the money supply. Yet, the vast population of lenders in the financial markets are not fooled by Federal Reserve Board statistics; only journalists, number-crunchers, and Treasury department undersecretaries are fooled.

WHY RATES ARE HIGHER FOR THE LITTLE GUY

In my description of the capital markets at the beginning of this testimony, I made the point that the growth of financial institutions was a process of persuading savers to put their extra wealth into depository institutions where bankers could make loans with it. The role of the banker was to use his judgment to put the money to work in its most productive investment. The main difference between a banker and any other investor is that a banker looks at a broad cross-section of businesses, and a divers set of businessmen-entrepreneurs, to form his judgment. The businessmen-entrepreneurs specialize in marketing, new-product development, or production efficiencies. The banker takes a wide-spectrum view, and the businessman-entrepreneur takes a focused, intensive view. Of course, there are also wealthy individuals, or venture capital firms, that do investment banking either for their own account or in cooperation with other accumulations of capital; and bank trust departments sometimes get into natural resources, and suchlike.

The main point of the distinction I want to make is that the "banking relationship" is more important for the small businessman than for the larger business. The corporate paper market, which has grown almost 50 percent just since the beginning of 1981, is available to the larger business firm, but not to the smaller one.

The "banking relationship," however, is becoming an increasing problem for small businessmen because the commercial banks themselves are in serious trouble in the United States. The money supply is not tight, as high interest rates reveal; but the flow of funds is not going into the small or middle-sized banks that typically finance small businesses. This is the consequence of fifty years of rigid banking regulation that is today strangling depository institutions in the United States.

Chairman St Germain of the House Banking Committee published a very interesting report earlier this year, in which he demonstrated that the so-called prime interest rate no longer has any specific meaning to bankers. At best, the "prime" is the mode of a statistical distribution of the interest rates charged to the banks' customers. The most-favored customers of the bank get a rate significantly below "prime," and the less-favored customers get a rate significantly above "prime." The important thing to note about these statistical distributions, however, is that the most-favored customers are the larger businesses that enjoy the alternatives of several different banks, or even the Eurodollar market, or the commercial paper market. Naturally, the banks will cut their rates below "prime" to get the business of these customers who have a higher elasticity of demand. In these cases, it is not the "bank relationship" that matters to the customer, it matters to the banker. For the customers who are charged rates above the "prime," the elasticity of demand is much lower. The small shopkeeper may only have one bank. He can't go to the Eurodollar market; he can't issue commercial paper, which might be picked up by some money-market fund.

Yet, the banks—and the thrift institutions, credit unions, etc.—are feeling the pinch of overregulation themselves. The small savers have discovered the innovations of the financial services industry. They have been taking their money out of the older, regulated depository institutions and placing it where it will keep them ahead of inflation. They are behaving just like rational lenders ought to behave. On the short end of the stick are the regulated depositories, and the small businesses that only have the few sources of funds. The solution, of course, in spite of the myopia and paranoia of the small bankers who believe that deregulation will deprive them of "independence" or increase some irrelevant statistic called "concentration" is immediate deregulation of their industry. Let them compete on equal terms with the new entrepreneurs in the financial services industry. If you want to solve the problem of access to capital for the small business in your districts, you will support initiatives such as Senator Jake Garn's deregulation bill—and you will push even farther than that too.

There was an article in The Washington Post a few days ago about a small company in Wisconsin that borrowed about $100,000 from its own employees in order to repay bank loans and obtain lower financing costs—in effect, cutting out the middleman and sharing the funds with its own workers. The State of Wisconsin, however, one of our more "progressive" States, has taken the company to court for violation of the securities laws. It seems that it is illegal to raise that much money from an "investment offering" as the small company did. How ironic! Here is just one more example of the way in which laws and regulations that are supposed to protect the small businessman, the small investor, or the less versatile members of our society actually function like boobytraps to injure the objects of the protection. The new book edited by Robert W. Poole, Jr., president of the Reason Foundation, Instead of Regulation (Lexington Books, 1981) continues an excellent chapter by Prof. George S. Benston of Rochester University on the U.S. Securities and Exchange Commission that proves that it has exactly the same kinds of harmful effects on small business nationwide (and without offsetting benefits of any kind).

THE SOLUTION: FASTER, MORE RADICAL DEREGULATION

We live in an advanced technological age. Citizens of the United States are among the best educated in the world. Each and every one of us has a keen appreciation of the devastation that inflation can cause our savings, and we pay attention when some new way to earn more money on our savings is advertised to us on television. The problem that small business faces when it goes to the bank for capital financing is that our capital markets are regulated on the distribution end, but not on the accumulation end. The small saver can put his funds into a money-market account in New York (or Zurich, London, or Hong Kong) with the greatest of ease. Yet, the small businessman who might want to borrow the funds that may have been saved by the citizens of his hometown cannot fly off to Zurich, London, or Hong Kong to submit a small loan application. The only way the neighborhood banker can compete with the international flow of funds is to buy them from some larger wholesale banker in a money-center city. All down the line, there is an added surcharge. This is the cost of our current set of laws and bank regulations in the United States. Ten years ago, eight of the twelve largest banks in the world were in the U.S. Today, only two of them are.

The small, protected banking industries in those States that forbid branch banking, that lobby in their State legislatures and in Congress against proposals such as Senator Garn's bill, are the real enemies of every other small businessman in the United States

Yet, the root of the problem with regulated financial markets in this country is even more fundamental. If the U.S. dollar were not losing its purchasing power—if it had not become, in the eyes of lenders, an inferior vehicle for preserving their ability to command real goods and services at some point in the future—perhaps the deregulation of our financial services industry would not have become so urgent. Adam Smith once wrote that critics of public policy decry the ruination of the nation, "but there is a lot of ruin in a nation." He wanted to reassure his readers that human society is highly adaptable; the people can cope with almost any kind of bad policy, although the economic system might be less efficient and produce more wasted resources than under wise policies.

Today, however, I come before you with a more urgent message. Our financial system is fatally flawed, with a defect that goes back to the founding of the Republic. And this defect, I am afraid is also a defect in the orthodox economic theory that dominates our universities. Since the days of Aristotle economists have believed that money is created by government; that a sovereign power must have a monopoly of its currency; and that to facilitate the exercise of this sovereign power, a government must have a central bank.

When Adam Smith wrote the Wealth of Nations (1776), Scotland had a free banking system without a central bank; no bank had any special privileges. Smith recognized free commercial banking's contribution to economic growth. David Ricardo, however, writing in England about forty years later, preferred a monopoly central bank. His students followed his lead. John Stuart Mill favored laissez-faire in everything except banking. His description of the Scottish competitive banking system in an 1826 article indicates that he didn't know its details; this error was repeated in an 1833 article. The English economists studied the operations of their own legal institutions to observe the economic process, and did not recommend radical changes—like abolishing the Bank of England's monopoly, established in 1694.

The economists in the British Neo-classical School of Economics, which spawned both John Maynard Keynes and Milton Friedman, just take the necessity of a central bank for granted. At the turn of the century, when the banking system in the United States was seen as needing reform, the solution they recommended was to create a central bank—not to revise the National Bank Act to make banking more competitive; they recommended that it be more centralized!

The theory, known as Monetarism, that says we must control a statistical series called M1-B, or M2, comes directly out of this British Neo-classical School of Economics. The idea that you need a central bank to control the quantity of money goes back to David Ricardo, but the unanswered question is, "How do you control the central bank?" (Ricardo's answer was a gold standard, but that is another subject—and the source of much controversy today.)

Adam Smith, and Walter Bagehot, wrote about free commercial banking and the beneficial effects for business. In the days of their research, even the largest business would probably be seen as a small business today. I have discussed, above, how inflation and the regulation of our banking and financial system have led to our current problems. The particular methodology of the modern high priests of the British Neo-classical School of Economics can not offer any particular answers to the present disintegration of our capital markets—because they believe that statistical time series are the essence of economic science. Consider the statement of Milton Friedman, writing in Newsweek, Sept. 21, p. 39:

"For each month since 1970 [a chart] plots a real interest rate, the difference between the average rate of interest on a three-month Treasury bill and the rate of inflation in consumer prices over the prior three months. . . ."

Notice the way in which Prof. Friedman uses a time series of data about consumer prices in the past to subtract a sum from a time series of T-bill rates—which were the anticipated rates of inflation by T-bill purchasers at the times when such T-bills were actually purchased. I do not quarrel with the definition of the "real" rate of interest—the difference between the nominal or market rate and the depreciation of the value of the dollar—but I would argue that Prof. Friedman should have looked consistently at the same time horizon (the future, in each case); and he should have used a measure of the capital markets, not the Consumer Price Index, which measures a different sector of human behavior. It is no wonder that the students of the British Neo-classical School of Economics have no answers to the present crisis in our capital markets.

TWO REAL-WORLD EXAMPLES WHERE DEREGULATION WORKS

Because I know you don't want to listen to a dry criticism of esoteric issues that may only concern professional economists, let me end with two real-world examples where free and open competition—not just among banking institutions, but also among currencies—today produces a healthy, non-inflationary environment with reasonable interest rates.

First, in Switzerland where the Swiss franc is the most stable monetary unit in the world. You have heard that this is because the Swiss bankers have a lot of gold, but that is not the reason because the Swiss franc is not convertible into gold. You have heard that the Swiss central bank pursues a very tight monetary policy, but that is not true because the Swiss central bank does not attempt to control bank reserves or influence the lending policies of individual Swiss banks. What does Switzerland have that the United States does not have? In Switzerland, the banks operate in a competitive foreign exchange environment, in which any depositor or borrower can keep his balances in any currency he chooses. By observing the supply and demand of different currency units, the Swiss bankers can easily and efficiently manage the supply of Swiss francs to keep inflation near zero and interest rates at about 2 to 3 percent.

Second, in Hong Kong. The Hong Kong dollar is managed entirely by the free market; there is no central bank. The rate of inflation is more volatile in Hong Kong, because it is more dependent upon capital inflows and outflows than Switzerland, and it is located in a more rapidly growing area of the world, where aggressive and optimistic entrepreneurs are more willing to bid up the prices of the capital goods they know they can put to economic, productive use. But the point of this example is that a central bank is not part of the economic and financial system. The British Neo-classical School of Economics cannot apodictically claim that the way to control inflation and bring down interest rates is to rely upon the Federal Reserve to control M1-B.

What the examples of Switzerland and Hong Kong do tell us, however, is that free and open competition in a deregulated market for capital and financial services is the way to control inflation and to enjoy the lowest possible interest rates.

Thank you, Mr. Chairman. I will be pleased to answer any questions that you or Members of the Subcommittee may have.

The current legal and regulatory structure defining depository institutions is becoming irrelevant due to changes in the marketplace. In its own interest, the banking industry should take the lead in supporting repeal of Glass-Steagall and McFadden-Douglas.

Deregulation of Banking: How Far, How Fast?

JOE COBB

The retail banking industry is about to experience a major transformation, not as a result of any changes in legislation but due to freedom of consumer choice and the increasing use of electronics in our financial system. The survivors in this coming industrial shake-up will be those who develop new management strategies to cope with a changing economic environment; the victims will be those who cling to a hope that protective regulations can save them from competition.

In developing an adaptive, aggressive management strategy in this changing market, it is most important that an institution understand what its business really is—what its customers really want. The history of the railroads is instructive. Fifty years ago, they refused to recognize that consumers wanted "transportation services," not just rail service. Railroads sought and obtained regulation of trucking by the Interstate Commerce Commission, but they failed to adapt by taking advantage of the new technology themselves. The railroads made a fatal error, and the development of the interstate highway system to accommodate motorized freight and passenger travel finally phased most of the railroads out of the economic life of the nation.

To avoid the experience of the railroads, bankers must recognize the fundamental changes evolving in their own industry. Retail banking is in the center of the "financial services industry." In the future, customers will want a comprehensive range of financial services from each supplier, not just a fragmented selection from many different suppliers—which present, obsolete regulations enforce. Individuals and corporate customers not only fail to understand the legal distinctions that differentiate traditional financial

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institutions today, but more important, they do not care. These customers want a full line of financial products and services made available at the lowest cost and greatest convenience. If they cannot get them from traditional financial institutions (depository institutions), they will take their business elsewhere—and they are doing just that. Walter Wriston was quoted in *Time* magazine, June 8, 1981, "Americans are not stupid. They have been seeking a better return on their money and getting it."

Economic theory tells us that competition is essentially a process of consumer choice, as individuals select among their opportunities to satisfy various needs or preferences. It is not important that different ways to satisfy consumer demand may be classified by government statisticians as "the same industry" or as a different line of business. The recent experience with competition between depository institutions and money market mutual funds should be instructive. The statutory restrictions on competition that prevent traditional depositories from offering new products does not protect them from competition—the regulatory environment *prevents* them from engaging successfully in competition. The growing recognition that regulations are a barrier to survival, not assurance of that survival, will generate growing demands from the banking industry itself for deregulation.

As competition and inevitable deregulation affect the rates of liabilities and yields on assets, banks will be forced to concentrate on the cost and efficiency of providing intermediary services. Pricing strategies will have to shift from balances to fees, in an effort to minimize transactions costs. Just like any other service business, the banks and other institutions will be purchasing raw materials (deposits and other liabilities) and selling finished goods (loans, investments, and other services) in a competitive market. With competition from virtually all types of depository institutions, price equilibrium will ultimately result in spreads between the purchase and sale of funds (or goods) being relatively constant, but small. Because the prices of raw materials and finished goods will be virtually identical, with some exceptions, differentiation among various providers of the financial services will result largely from efficiency in product delivery. Different segments of the market will have different needs or preferences, and the successful management strategy will, in each case, identify the market segments where a comparative advantage can be developed. Banks and other financial service providers will become "relationship oriented" rather than product oriented.

The Emerging Price Revolution

The Depository Institutions Deregulation and Monetary Control Act of 1980, among other provisions, requires the Federal Reserve to begin pricing its money-transfer services on a full-cost basis, including float. This will create serious cost pressures for banks, and can only lead to an end of free checking, free currency, and related services—and thus to explicit pricing.

Whereas in the past, the ability to earn an interest rate differential on depositors' idle balances was a source of revenue to cross-subsidize the services provided to customers on a gratuitous basis, this revenue is diminishing as depositors tend to move funds more frequently in response to market interest rates. Moreover, with the elimination of free support-services from the Federal Reserve, it will become increasingly necessary to recover the costs of convenience services directly at the "point of sale." The squeeze on the financial intermediation side of the banking business will be severe and banks will begin to reduce their dependence on credit extension in the 1980s, drawing increasing proportions of their annual revenue from "fee for service" pricing.

> *. . . with some exceptions, differentiation among various providers of the financial services will result largely from efficiency in product delivery.*

This scenario seems grim only if one holds a narrow view of retail banking—that banking is primarily an interest rate differential business. A broader view of banking, that of financial services, would suggest that one adjustment to the changing environment would be to accept a diminished role for the traditional interest-spread

If there were no competitive pressures on retail banking's money transfer services from other . . . institutions, . . . bankers might safely ignore the application of electronics to such services.

business and to emphasize the broadest range of services available from one, familiar institution. Customer convenience, and competitive prices, will be the secret of success in the future. This will actually be a healthier orientation for banks because not only will they offer a full range of financial services but all services will receive equal management attention.

Service income will be derived from fees charged to customers, forcing management to determine, far more precisely than now, how much it costs to produce each service and ensure that each service is priced properly. This approach may allow banks to become less dependent upon purchased money as deposits continue to decline. Banks will turn to electronic technology to deliver these financial services, because of cost and competitive pressures as well as a greater recognition of the business banks are in. Banks should find that the financial services business equates to information processing, which can only be handled efficiently, securely and conveniently by electronic technology.

For over a century or more, money transfer services provided by banks have been largely unaffected by technological progress. Commercial banking money transfer services continue to be moved predominantly by paper technology. If there were no competitive pressures on retail banking's money transfer services from other financial institutions, credit card companies, mutual funds, and data processing and communications companies, bankers might safely ignore the application of electronics to such services. There is competition, however, and corporate EFT services such as automated clearinghouses are at the forefront of changes banks are making as they prepare for the future.

The nature of banking is evolving into one of income earned from the flow of funds through the economy, rather than from financial intermediation. In the 1980s, money-center banks will offer a full complement of financial services nationwide as will other financial institutions. These services will be delivered primarily by electronic technology and income will be derived primarily from fees and the flow of funds, and fast turnaround, rather than balances. The most important detail of this scenario, moreover, is that the services will be as near as a customer's telephone, so McFadden-Douglas constraints will become irrelevant. Since firms with different corporate charters will offer such close substitutes for each other's services, the Glass-Steagall distinctions will become irrelevant. Finally, arguments against repeal of these anachronistic laws based on the "market concentration doctrine" are already irrelevant.[1]

Institutional Offerings

This vision of the future of retail banking is not really dramatically different from the current situation. It is just an extension of what took place in the 1970s. The major difference is that the 1970s were a period of experimentation, whereas, although experimentation will continue, the 1980s will be a period of implementation and exploitation of established new procedures. What was taking place under the surface in the 1970s will come out into the open in the 1980s.

The current regulatory structure simply no longer applies to the financial services industry as it exists today. It applies only to commercial banks, thrifts and securities firms and it is, therefore, inhibiting such institutions. Foreign banks and electronic terminals are straining the credibility of geographic limitations on deposit gathering. NOW accounts, share-draft accounts, automatic transfers between savings and checking, money-market funds, and Merrill Lynch's Cash Management Accounts clearly violated the letter and spirit of interest rate controls, but the combination of the Monetary Control Act of 1980 and recent judicial decisions have legalized them. Share drafts, electronic terminals, and telephone bill-paying services offered by thrifts and credit unions are functionally equivalent to checks. Merrill Lynch's CMA accounts and commercial banking's interest in private placements and the commercial paper market blur the legal distinctions between commercial and investment banking in Glass-Steagall.

Other examples abound of nonbanks' offering traditional bank services. Finance companies make cash loans to individuals and businesses, and, in some cases, issue small denomination deposit-like liabilities in competition with depository institutions. Life insurance companies sell insurance policies that cost more than the actual life insurance protection warrants and place over-charges in a savings-type account that earns interest and permits withdrawals. Retailers compete with banks in providing consumer credit—Sears Roebuck entered competition with banking in 1911. All of these activities are carried on outside the regulatory structure, which simply means that the marketplace has ignored the regulatory structure. Banks themselves, through holding companies, loan production offices, and Edge Act corporations, have all played a role in the erosion of regulations, so it is curious to see many bankers today continuing to support them.

Foreign banks and electronic terminals are straining the credibility of geographic limitations on deposit gathering.

Survival in a Time of Change

There is a principle from the theory of finance that should be of some value to bank managers who might still be uncertain about how to address the changes that will be required. Since the 1930s the banking business has been constricted by rigidly defined markets for limited-service institutions. We know, however, that a small, concentrated portfolio of investments is more risky and has a greater variance of return than a larger, diversified portfolio. There are two ways that this principle applies to the strategic planning that bank managers should be doing to adapt and survive in the new, competitive marketplace. First, the principle suggests that a particular institution should broaden its product-line, or find ways to offer additional customer services, even those that seem unconventional: a real-estate office in one corner of the lobby, under separate ownership if necessary; an insurance agency in another corner of the lobby; management consulting, computer software and accounting-services packages for small business. Only the managers' imagination should limit their experimentation. The comparative advantage that a bank might have in providing all of these services in one place starts with the bank's traditional identification with prudent financial management; and new customers are then attracted on the basis of one-stop shopping.

Second, the principle of a diversified portfolio applies to opportunities for outright merger among financial institutions that may offer different specialties. To the extent that present law and regulations may restrict this kind of diversification, it is clearly in the interest of the entire banking industry to have the laws repealed. Since there is obviously no hope at all for passing new laws to restrict Merrill Lynch, American Express/Shearson, or Bache/Prudential, the industry should take direct action now—or procrastinate until it may be too late. Perhaps the ideal form of deregulation would wipe out any and all legal distinctions between financial corporations, including depository institutions, and non-financial corporations. The efficiency of capital markets and the reduction of overhead costs by industry could be fostered. The ability of a nonfinancial corporation, say, a small manufacturing company, to acquire, say, a failing thrift institution, would bring benefits to both firms. By running its payroll through the thrift institution, the manufacturer would be able to economize on its minimum working capital because employees might tend to leave most of their paychecks on deposit and pay them out by check or electronic transfer over the entire two-week period. The thrift institution already has some specialization in financial management, so it could supply the manufacturer with accounting services and perhaps attract additional working capital from nonemployee depositors. To the extent that the thrift institution's assets were in the form of long-term, low-yield mortgages to the manufacturer's employees, their loyalty and commitment to productivity could be enhanced. This appeal could be used to hold funds on deposit in the face of slightly higher yields offered by money-center banks that might try to use nationwide televised advertising to attract funds, as the money-market competitors are already doing.

In states that have traditionally prohibited branch banking, a more aggressive process of linking unit banks under a common name or under cooperative business agreements should be encouraged, or attempted, in spite of apparent adverse legal regulations. The legal environment is changing rapidly, but only after a period of slow recognition that the marketplace has made it irrelevant. The statutes, both state and national, are needless stumbling blocks for some of the players in the competition but not for others. The manager who waits for the law to change before attempting to attract customers will be the last person across the finish line; such a manager, looking to the future, should offer the new product or service, advocate that the laws be repealed to legalize the product or service, and at the same time attract the political support of those very customers who would like to buy the service. This recommendation is not radical; it is precisely what has happened in the past ten years, and knowledgeable public affairs executives in money-center banks and other competing financial-services firms have become very skillful in exactly this issue-management process. Legislatures respond to public clamor for change; but the public will only take an interest in such change if it can see that it is missing something that might otherwise be available. If that "something" is more interest on deposits or less costly loans, the appeal is very, very powerful.

The smaller institutions will always have one comparative advantage over the more distant, larger ones: a more specialized knowledge of customers and community interests. In the financial services industry, default is the principal risk. And the key information for estimating default risk is entirely judgmental—a human quality that no computerized software package will be able to replace. It was this factor, in the main, that has led to the continued growth of smaller, upstate banks in New York following the movement to statewide branching a few years ago. To the extent that financial services become more and more similar to information-processing services, it is important to remember exactly where economic information comes from: it only comes from individual human judgments about relative values and opportunities.[3] If this were not the basic truth in economics, our society would long ago have turned to macroeconomic central planning and all financial institutions might as well be nationalized, become branch offices of the Federal Reserve Banks, and issue loans at the prevailing discount rate to all customers without distinction.

Banks themselves, through holding companies, loan production offices, and Edge Act corporations, have all played a role in the erosion of regulations, so it is curious to see many bankers today continuing to support them.

Looking at the Future

The banking environment, as we have argued, will differ significantly from the traditional view of banking. It will not differ so much, however, from the environment that evolved over the last decade due to competitive and technological pressures. In the 1980s, we will witness a dramatic acceleration of the competitive and technological forces that surfaced in the 1970s, accompanied by the following environmental changes:

- The artificial distinctions among depository institutions will disappear entirely.
- Geographic limitations on deposit-gathering will be relaxed as they become increasingly irrelevant.
- The distinctions among depositories and other financial institutions will become further blurred.
- Depositories will begin a consolidation process that will be much less severe than most people think.
- Depositories will price their products explicitly and at full cost, at the margin; the legal limits on interest rates will be abolished.
- Interest will be paid on transactional balances.

- Electronic funds transfers will be a major catalyst in the transition to this more competitive and efficient environment.

These changes will not occur overnight, nor will they occur all together, but they are logical outcomes of powerful trends that are gaining momentum. Regulatory reform legislation will play a lagging rather than a leading role. The powerful competitive and technological forces already at work will cause the changes, not any active decisions by regulatory authorities.

The International Banking Act and the Monetary Control Act combined with competition from foreign banks will put additional pressure on efforts to relax geographic barriers. It will become increasingly difficult to prevent electronic technology from crossing state lines. The first step will probably be to permit ATMs to cross state lines—on a regional basis, as in the Washington, D.C. area today, and then on a nationwide basis—as with American Express Co. travelers check machines today. Corporate EFT is becoming one of the most important services that large banks offer. Reciprocal agreements between states, allowing interstate banking to occur, may focus pressure to repeal the Douglas Amendment.

Mandatory membership or the holding of reserves with the Federal Reserve may cause some conversion from state to national charters, which would heighten pressures for interstate banking. The McFadden Act may or may not be amended. The important thing to remember about McFadden is that interstate banking can occur without changing it. Some of the other changes listed above and a more pervasive use of EFT are all that are needed.

Reciprocal agreements between states, allowing interstate banking to occur, may focus pressure to repeal the Douglas Amendment.

The ultimate, perhaps utopian, deregulatory reform would be the repeal of mandatory reserve requirements.

The ultimate, perhaps utopian, deregulatory reform would be the repeal of mandatory reserve requirements. From the history of banking in the United States, it is clear that required reserves do not increase the security of depositors. Required reserves are merely a discriminatory tax on depository institutions because they are required to sterilize a portion of their assets, and the Federal Reserve System and the Treasury reap the benefits because they earn interest on the reserves held. A recent proposal by Paul A. Volcker that money market funds should also keep their reserves at the Fed was met with disdain by the Senate Banking Committee, so the "unlevel playing field" will continue as long as this anachronistic rule—held over from the days of mercantilism when bank charters were granted only for political reasons—is part of our banking system.[3]

In an era of rapid international economic growth, economists are becoming increasingly aware that the world is one, integrated transnational economic system. The financial institutions of this world-wide economy compete in an essentially unregulated environment, except in the United States and a few other countries. Whereas as recently as ten years ago, eight of the dozen largest banks were American, today only two of them are. The financial center of Asia—Hong Kong—thrives without bank regulations or a central bank. It is not in the public interest for the United States unilaterally to kill off its most important financial services institutions, and it is not in the long-run interests of bankers to participate in this auto-da-fé out of fear of competition. Leaders in the industry already recognize this fact of life.

Notes

1. The "market concentration doctrine" says that concentration in a line of business is bad because it leads to monopoly pricing and misallocation of resources. The empirical research that destroys this hypothesis can be found in Yale Brozen, "The Persistence of 'High Rates of Return' in High-Stable Concentration Industries," *Journal of Law & Economics*, XIV (Oct. 1971), 501–12. See also Brozen's earlier study, "The Antitrust Task Force Deconcentration Recommendation," *J. Law & Econ.*, XIII

(Oct. 1970), 279–92 (available as a reprint from the American Enterprise Institute, Washington, D.C.).

The principal fallacy in the argument presented by Thomas F. Bolger, "The McFadden Study: An Unsound Proposal for Community Banks," in this journal, March 1981, is in the definition of the relevant market strictly in terms of geographical area and charter authority, not in terms of the consumers' perceptions of close substitutes for banking services. His general argument is that market concentration would increase. He failed to ask the more important question: So what?

2. *Cf.* F. A. Hayek, "The Use of Knowledge in Society," *American Economic review*, XXXV (Sept. 1945), 519–30; James Buchanan, *Cost and Choice* (Chicago: The University of Chicago Press, 1969); and Thomas Sowell, *Knowledge and Decisions* (New York: Basic Books, 1980). All of modern, scientific economics is founded on subjective marginal utility and the concept of opportunity cost. The insight that economic information is essentially decentralized, and not capable of being reduced to statistics, nor capable of discovery outside of the market process, is the basic insight of Ludwig von Mises, *Human Action* (Chicago: Contemporary Books, 1966). His *The Theory of Money and Credit* (Indianapolis: Liberty Classics, 1981) is a classic, first published in 1912, with which every person in the financial services industry ought to be familiar.

3. An excellent history of banking in the United States and in Europe can be found in Vera C. Smith, *The Rationale of Central Banking* (London: King, 1936). This important book has been long out of print, but its concluding chapters are available from the Committee for Monetary Research and Education, Inc., Postal Box 1630, Greenwich, CT 06830; Monograph 34, June 1981, $3.00. This book is all the more important because it traces the intellectual history of banking regulation in theory and practice from the 17th century to the 20th. It shows how bank regulation originated in the attempt by political parties to reward supporters, and how the centralization of banking is in fact grounded on an error in 19th century economic theory that has yet to be corrected. As background information for the preparation of a management strategy for survival in the 1980s, a history of the ideas that are the source of the problem is important.

Mr. Nowak. I just would like to mention that Mr. Cobb has a particularly outstanding background. He has an A.B. and M.B.A. from the University of Chicago, where he specialized in the theory of finance and industrial organization. He has published works in many journals, including the Journal of Retail Banking, Barrons, the Illinois Banker, and Cash Manager. He's editor of the Monograph Series of the Committee for Monetary Research and Education in Connecticut. We welcome you before the subcommittee, Mr. Cobb.

Mr. Cobb. Thank you, Mr. Chairman.

I'm appearing here today representing the Council for a Competitive Economy. The council is a national membership organization of businesses and individuals dedicated to a free, competitive, market economy, unhampered by regulations, taxation, protectionism, subsidies, or special privileges for any business or labor organization.

I'm speaking today on behalf of our 1,500 members in all 50 States. Most of our members are owners of small businesses or individuals working in middle management of larger companies who would like someday to be self-employed as proprietors of small businesses.

High interest rates in our economy today are the symptoms of a disease. The disease, in particular, is the degeneration or regression of our capital markets. This is the central point I want to make in today's testimony. The efficiency of our capital markets is being destroyed. The first victims of this wholesale destruction are the small businessmen, particularly those in the interest sensitive industries like auto dealerships and homebuilders, whose basic position in our society you Congressmen are here to defend.

Yet, the process of destruction of our capital markets will not end with the small businessman. Mr. Stoner has commented about the businessmen he is acquainted with who may be doing all right temporarily but their businesses are not expanding, and this disease that I'm describing will affect them next year or the year after if something isn't done.

Even the larger businesses will eventually be affected by this in a very adverse way. In the last analysis, a free society will become impossible because you can't have a capitalist society without long-term capital markets. The capital markets are the only way a free market can plan for the future.

In my statement today, I want to address three questions. Why are interest rates higher today than ever before in the United States? Why are interest rates higher for small businesses than for large businesses? And why must the solution be found in more rapid deregulation and not new regulations?

I want to comment very briefly on the recommendation by Frederick Napolitano of the National Association of Homebuilders, recommending that you extend the Credit Control Act. I think that would be absolutely the wrong thing to do. It would send absolutely the wrong signal to the capital markets, because what the capital markets need is a more thoroughgoing deregulation.

I believe that in my analysis of these three questions I think I can also show you why most professional economists who may appear before these committees of Congress may not understand.

They may come to you in 1 month and predict interest rates will come down and then they come back 3 months later with egg on their face, with no explanation why interest rates have not come down.

Interest rates are set competitively by millions of people in the capital markets. Interest rates are not set by the Federal Reserve Board. Interest rates are not set by Government fiscal and monetary policy. Interest rates are set in a competitive process involving literally millions of people that have saved funds and placed those funds into the markets, expecting a rate of return, and by borrowers, some of whom, of course, may be desperate, but nevertheless, borrowers who are willing to pay those interest rates. Otherwise, there is no transaction and there is no rate of interest to report to some Government statistics collector.

The lender in today's market is most interested in something quite different than the scarcity of dollars in the marketplace. You made in your opening remarks the statement that the Federal Reserve Board is pursuing a tight monetary policy. I'm sorry, sir, but it's pursuing a very loose monetary policy. If you look, for example, at yesterday's Wall Street Journal and the statistics they have on the editorial page, the point I'm trying to make will be illustrated there by a nice little chart.

The lender wants to know how many real goods and services the same amount of dollars that he may lend you today will buy in the future. Why should anybody lend money? Why should anybody give up the real goods and services that the money might buy today, especially if there is a genuine fear by the lender that what he gets back in the future won't buy as much?

An interest rate of 20 percent is just another way of saying that a lender will agree to give you command of real goods and services, his share of real goods and services, if you will double the amount of dollars in 3 years. An interest rate of 10 percent implies that the amount of dollars will double in 7 years. An interest rate of 7 percent implies that the amount of dollars will double in 10 years.

Unfortunately, in this age of inflation, the word dollar has no meaning. It has a pronunciation. It has a spelling. It even has a connotation. But it has no meaning for any time period longer than about 10 minutes. Therefore, in today's capital markets, lenders are willing to enter into contracts with borrowers, stated in terms of dollars, only for shorter and shorter time periods and then only if they can be assured that the number of dollars will at least double in 3 years, because the very word that we use to quote prices has no meaning over a longer period of time.

The fact is, as I said, that the money is not tight, but it's quite loose.

The President and the Secretary of the Treasury have paid too much attention to Federal Reserve Board statistics about the money supply, in particular M1-B. These statistics are very misleading because each narrowly defined monetary aggregate does not take account of nearly perfect substitutes in the money market. The fact alone that M1-B is near the bottom of its target range but M2 is near the top of its target range tells you that something is wrong with the definitions of the money supply.

Yet, the vast population of lenders in the financial markets are not fooled by Federal Reserve Board statistics. Only journalists, number crunchers, and Treasury Department Under Secretaries are fooled.

The main point of the distinction I want to make about why interest rates are higher for the little guy is that for the small businessman, the banking relationship is his most important relationship to the capital markets. It's more important for the small businessman than for the larger businessman. The corporate paper market, which has grown almost 50 percent since the beginning of 1981, is available to the larger business firm but not to the smaller one.

The banking relationship, however, is becoming an increasing problem for small businessmen, especially homebuilders, because the commercial banks themselves are in serious trouble in the United States. I use the word "commercial bank" in a very broad sense, to include thrift institutions, credit unions, and also insurance companies and other institutional lenders.

The money supply is not tight, as the high interest rates reveal. The lenders are willing to lend money, at 20-percent interest rates. But the flow of funds is not going into the small or middle-sized banks that typically finance small business. Money is coming out of the thrift industry. This is the consequence of 50 years of rigid banking regulation that is today strangling depository institutions in the United States.

The small saver can put his funds into a money market fund in New York or, for that matter, in Zurich or London or Hong Kong, with the greatest of ease. Yet, the small businessman who might want to borrow the funds that may have been saved by the citizens of his hometown, cannot fly off to Zurich or London or Hong Kong to submit a small loan application.

The only way the neighborhood banker can compete with the international flow of funds is to buy them from some larger wholesale banker in a money center city. All down the line there is an added surcharge. This is the cost of our current set of laws and bank regulations in the United States. Ten years ago 8 of the 12 largest banks in the world were in the United States. Today, only two of them are.

The small, protected banking industries in those States that forbid branch banking, that lobby in their State legislatures and in Congress against proposals such as Senator Garn's bill, S. 1720, are the real enemies of every other small businessman in the United States today. It's the seeking of special privilege by one industry that's harming every other industry.

Today, however, I come before you with a more urgent message. Our financial system is fatally flawed with a defect that goes back to the founding of the Republic, and this defect, I'm afraid, is also a defect in the orthodox economic theory that dominates our universities. Since the days of Aristotle, economists have believed that money is created by government, that a sovereign power must have a monopoly of its currency, and that to facilitate the exercise of this sovereign power, a government must have a central bank.

The theory, known as monetarism, that says we must control a statistical series called M1-B or M2 comes directly out of this British neo-classical school of economics that is the economic orthodoxy in the United States today. The idea that you need a central bank to control the quantity of money goes back to David Ricardo, but the unanswered question is how do you control the central bank? Ricardo's answer was a gold standard, but that is another subject that I'm not going to get into today, a subject of much controversy.

Interestingly enough, Adam Smith, who founded the science of economics before David Ricardo, wrote in Scotland in 1776 where there was no central banking institution.

People in the British neo-classical school of economics include John Maynard Keynes and Milton Friedman. I think that's one of the problems why eminent gentlemen such as Jack Carlson, who testified earlier today, would reach a conclusion believing that the money supply is tight and believing that the solution to the problem is that you have to delay the tax cut or speed the budget cuts and, because he doubts the budget will be in balance anytime soon, he looks at the markets and says interest rates are very high because lenders are very scared.

But, I really think he misses the point there. If you look at the capital markets, you'll see that those people, the so-called quality borrowers that go into the markets, can get funds.

The Federal Reserve Board is supplying funds quite liberally in the M2 and the M3 categories. It's only the categories like M1-B that look tight. Now, the problem is that the definition of our monetary unit is evaporating. The lenders are aware of this. The long-term bond lenders have been burned so terribly bad in the past 5 years that they're all looking for 90-day maturities instead of 5-, 10-, 20-year maturities, and the problem is that in the United States today, because we are dependent upon the Federal Reserve Board and whatever it may do behind closed doors for our capital markets, we have no way of knowing, as we sit in Congress or as we look at the press, what they are really doing. The markets, however, understand that the quality of money is disintegrating.

I've studied institutional arrangements in places like Hong Kong, where there is no central bank. I've talked with people at the Swiss Embassy who have described the situation that occurs in Switzerland. You know that in Switzerland interest rates are about 2 percent. You know that the Swiss franc is the most solid currency unit in the world, and there are a number of theories that have been bounced around as to why this is true, and I want to present to you my findings.

People have said the Swiss bank policy is that of tight money, that they follow monetarism. But, that's not true, because the Swiss central bank doesn't try to squeeze the supply of reserves in the Swiss banking community. As a matter of fact, the Swiss central bank supplies each commercial bank in Switzerland with as many bank notes as it wants. Banks keep large inventories of bank notes in Swiss banks. But what Switzerland does have, of course, others have said is a large inventory of gold, but that's not the answer either, because the Swiss central bank will not convert the Swiss franc to gold upon demand if you walk in with a Swiss bank note. They won't do it. So, gold isn't the answer either.

What they do have in Switzerland is a competitive banking environment in which each depositor can keep his bank balance in any currency unit he chooses. There is no legal tender monopoly for the Swiss franc in Switzerland. This means that the Swiss banking community, in a decentralized way, knows when the quality of the Swiss franc is beginning to deteriorate. They know that if depositors are switching their funds from Swiss francs to U.S. dollars or from Swiss francs to deutsche marks, that they have to contract lending in terms of Swiss francs, and this is how the Swiss banking environment, a competitive environment, regulates itself.

An even more interesting case is the case of Hong Kong because Hong Kong does not even have a central bank. Instead, you have about 700 banking institutions in Hong Kong, all of whom engage competitively in the loan making business and in the capital financing business, and they are able to determine, again, based upon the behavior of their depositors, as they convert funds from one numeraire to another, whether or not they have overexpanded credit or underexpanded credit, and interest rates in Hong Kong are also much lower than they are in the United States.

The important thing about Hong Kong, unfortunately, is that because it's a small colony, it is dependent upon international capital flows and world inflation also affects Hong Kong in a more severe way than it affects Switzerland.

I think that what we need to do in this economy today is look to some mechanism to put the Federal Reserve Board itself into a competitive environment. I think that if Americans had a freedom of choice to use any currency units they chose, including, if they chose, a gold coinage, that you would have an inflation rate that would drop near to zero, as it has done in Switzerland, and you would have interest rates of about 2 percent, as they are in Switzerland.

Now, I want to address very briefly the popular journalistic theory that floats around today that somehow it's the size of the budget deficit that's causing high interest rates. I know that Dr. Carlson made a reference to this. The theory is that somehow if the Federal Government is in the capital markets bidding for a lot of funds that you have a heavy bidding pressure and, of course, a limited supply and therefore the price of funds might go up. The problem is that this theory ignores the fact that the United States is only about one-third of the world economy and capital moves across international borders with the greatest of ease. There are no restrictions upon placement of funds by Americans in Europe, placement of funds in America by Europeans or Asians, and so the size of the U.S. budget deficit is absolutely irrelevant to the size of U.S. interest rates.

I've got a chart that I would like to—I have several copies here and if the clerk could pick some up and pass them to you—this data is from 1945 through 1982's estimated period of time. The budget and off-budget deficit or surplus as a percentage of gross national product, the publicly held national debt as a percentage of the gross national product, and the Aaa corporate bond yield, which I think is a very good proxy for what the market interest rate is.

[The chart referred to above follows.]

BUDGETS AND BONDS

	Budget & Off-Budget Deficit or Surplus (+) as % of GNP	Publicly-Held National Debt as % of GNP	Aaa Corporate Bond Yield
1945	22.4%	119.2%	2.6%
1953	1.9	62.2	3.2
1958	2.3	51.6	3.8
1968	3.0	34.8	6.2
1969	+0.4	30.7	7.0
1971	2.2	29.5	7.4
1974	0.4	25.1	8.6
1975	3.6	26.8	8.8
1976	4.5	29.2	8.4
1979	1.7	27.3	9.6
1980	2.9	27.9	11.9
1981	2.8	27.4	13.4*
1982^{e}	1.9-2.5	26.4	NA

*Jan.-Aug., seasoned bonds.

Mr. Cobb. You will notice that the budget and off-budget surplus as a percentage of GNP is not going up. It's remaining relatively constant. You will notice that the publicly held national debt is actually going down. And you'll notice that the triple Aaa corporate bond yield is now up around 13 or 14 percent.

So, the deficit doesn't explain high interest rates. Moreover, if you look at the testimony of Prof. Arthur Laffer before the House Ways and Means Committee on March 4 of this year, he points out in his testimony that the Federal Government is actually paying off the national debt through inflation. The principal value of the national debt is shrinking in terms of real goods and services. The Federal budget is in surplus at the present time in terms of real goods and services. It's only in deficit in terms of the unit of account which we call the dollar, and which as I pointed out earlier, has no meaning for time periods of longer than about 10 minutes.

Thank you. I'll be pleased to answer your questions.

Mr. NOWAK. Thank you very much, Mr. Cobb. Let me first of all get a couple of questions from Mr. Stoner. I think perhaps both of you could give your views on this. We talk about what has transpired over the last few years and I think some of the deregulation that has occurred has, in many instances, increased competitiveness. I sit on the Public Works Committee also and we went through the airline deregulation, the truck deregulation, and now we're going to be talking about the bus deregulation, and I assume that the banking deregulation bill will be moving forward to some degree.

As we talk about competitiveness, I wonder if you could just comment on the growth of the money market funds, that phenomena which has seemed to be shifting money from what was traditional sources for small business loans and homebuilding loans from the savings bank into these money market funds. Do you see that as having an effect on the kinds of credits that may be available out there in the future?

Mr. COBB. Yes. The money market funds represent an innovation in financial services because entrepreneurs in Wall Street investment firms recognized that they could create an investment vehicle for the small saver that would get around regulation Q. They were able to offer fund placement services to the small investor and then, of course, by advertising them, they were able to attract money away from the traditional depository institutions, thrift institutions, and commercial banks.

There was some talk earlier this year by Chairman Volcker of the Federal Reserve that perhaps money market funds should be brought under regulation. Of course, that was laughed out of court because so many small savers wrote you gentlemen of Congress and said, "Don't do that; it's the only salvation we have to earn a rate of interest that will preserve our money for us over time," as I pointed out, doubling it in 3 years or 7 years.

I don't think that there should be any attempt at all to impose restrictions or regulations on that sort of innovation because it's a way in which the businessman, entrepreneur, is able to satisfy a consumer demand and I think that's a totally ethical and moral act for a businessman to engage in.

What is unfortunate and bordering on the immoral, in my opinion, is when the thrift institution that is losing the funds, comes to Congress and begs for some sort of restriction to be placed upon his competitor, the money market funds.

Unfortunately, the thrift industry, of course, is under very heavy regulation and I think that the solution to this problem is as rapid as possible deregulation of all of the poor, unfortunate institutions that are today being crippled by the Federal Reserve and other regulatory bodies.

Now, the Federal Reserve requires each depository institution to keep a certain percentage of its assets on deposit with the Fed. That's called "the reserve requirement" of the bank or the thrift. This, unfortunately, is a discriminatory tax upon your traditional depository institutions and, of course, the small businessmen go to those for their loans. They can't go to money market funds for loans, and the money is being shifted in our economy by the choices of the small savers into those kinds of investment opportunities that are blocked to the small businessman, and it is a consequence of Government regulation that distorts the capital markets.

I identified not only the problem of the degradation of the value of the dollar because of loose money, but I also pointed to the structural rigidities in our capital market that make them even less accessible to the small businessman.

There was a story in the Washington Post about a Wisconsin employer who borrowed money from his employees and paid off his bank loans and then he was socked by the Wisconsin securities regulatory agency because under Wisconsin State securities laws he was making an unlawful securities offering to his employees. Now, here's an example of Government regulation in the capital markets that benefits nobody and openly harms the employees and the employer, that were trying to at least get together into a partnership arrangement to rescue the business that they all depended upon.

So, I think that money market funds are wonderful.

I wanted to point out that in Switzerland you don't have money market funds because commercial banks do that kind of business. In Hong Kong now they are developing money market funds because the Hong Kong Government since 1967 has stopped granting bank charters and so those entrepreneurs that want to start banks in Hong Kong now call themselves investment companies and offer money market funds.

You see, the entrepreneur in the market is smarter than the Government regulator and the only consequence of the Government regulation is to indirectly harm somebody else, like the small businessman.

Mr. **Nowak**. Thank you. Mr. Stoner, do you have a comment?

Mr. **Stoner**. Yes. I want to just add a comment to that, again, referring to the persons who I am associated with most of the time. There are available funds in the commercial banks. Yes, they are very costly. I mentioned in my testimony the one gentleman, however, and his firm is no larger than mine who's getting that money at prime. I have a line of credit with M. & T. at $100,000 at one point over prime. I'm not using it but it's there. The money is there if you can handle the cost.

Mr. **Cobb**. Mr. Chairman, let me add one point. Mr. St Germain had hearings in the House Banking Committee last spring to examine the meaning of the word "prime" as it's used by the banking industry and he discovered that the bankers themselves are retreating from that word. It's no longer the rate at which they offer their highest quality customers. It's simply a benchmark rate: They charge their lower quality customers, certain percentage points above it and they offer their genuinely preferred customers money at several points below it.

Now, the important difference is that the customers that get the offerings below prime are the very ones that also do have alternatives open to them in the commercial paper market or the Eurodollar market, and it's in the competitive areas and it's as a consequence of competition that interest rates are lower for those borrowers and it's as a result of the absence of alternatives that the interest rate is above prime, even for high quality businesses such as Mr. Stoner's.

Mr. NOWAK. Speaking of the effect of the money markets coming into being at this time, we've seen where the savings and loan industry, for example, has, I believe, about 26,000 banks out there. It's been predicted that in 4 or 5 years that number will shrink because of mergers or just going out of business to, I guess, about 6,000 and the 6,000, of course, will be much larger. I still have some feelings that an awful lot of people will be forced out of the banking business unless they can start to compete with the money market certificates and that, of course, would mean national banking of some kind without limitation either within the State or outside of a State.

We hear about Sears, Roebuck now coming into the opening of a money market fund and we also have seen the phenomenon of Merrill Lynch now buying up all the small business real estate companies that they can get their hands on, even with the depressed industry state. Perhaps now is a good time for them to start moving. But, Sears also has expressed an interest in getting into the opening up of real estate firms as well, I understand, to use their extensive marketing locations that they have already in place, as they have with the Allstate Insurance Co.

Dr. Carlson was talking about the problems that he foresaw in the merger phenomena and that the smaller businessman would eventually, one way or another, have to either merge or be forced out of business, because of competition by a larger firm who is able to take a loss for a period of time. Do you see that as any kind of a problem at all in those kinds of industries that could be subject to that kind of pressure?

Mr. COBB. I see one problem and one opportunity in that phenomena.

First, I do not subscribe to what is called in economics, "the concentration doctrine." The concentration doctrine is the theory that if you have only a few producers, somehow you're approaching a monopoly environment and therefore that's bad. Empirical research by Prof. Yale Brozen at the University of Chicago, which was published in The Journal of Law and Economics in 1970 and 1971, showed quite clearly that concentrated industries do not earn higher rates of return than unconcentrated industries and it's just a myth to believe that somehow the big guy is somehow also the powerful guy.

In a free market the consumer choices and the ability of consumers to buy or to refrain from buying from any particular supplier is your ultimate check upon any kind of economic power.

Now, the danger I see at the present time is that the thrift institutions and the small commercial banks are not permitted to diversify themselves in such a way that they could successfully compete. The problem is that Sears, Roebuck and Merrill Lynch are moving like racehorses in an area where the thrifts and the commercial banks would love to compete but the current laws and regulations forbid it.

Now, Merrill Lynch is in an ideal situation to buy up all those small real estate firms because, in the first place, those firms have inventories of land and buildings. Merrill Lynch has liquid cash.

Now, the land and buildings ordinarily would have been sold, I suppose, to individuals who would finance it through a thrift institution, but the cash that might have gone to the thrift institution has gone instead, through the voluntary placement of those funds by the saver, into Merrill Lynch, and the problem is, of course, that if you worry about any accumulation of power in the hands of somebody like Merrill Lynch, you should at least recognize that accumulation is happening only because the forces that might lead to decentralization have been prevented by Government regulations, and the solution is to open up the market. Let everyone compete. Let everyone compete on an equal footing. That means if you're going to have an unregulated money market fund, which is, of course, a very good innovation, you should also have an unregulated bank, and you should get rid of the discriminatory tax that the bank has to pay called its "required reserve" also.

Mr. NOWAK. Your statement about the deficit position is also interesting. The perception that's out there, of course, is vastly different from the statistical information would show, if you analyze it.

Mr. COBB. Yes.

Mr. NOWAK. I've gone over those figures before and looked at that percentage of debt to the gross national product and looked at different years when the percentage or where the deficit was large, and yet we had low inflation and low interest rates and there were some periods of time where the converse would be true.

Mr. COBB. That's correct.

Mr. NOWAK. So the correlation that is made does not seem to hold up under analysis and yet every time you read a statement in the paper from anybody on Wall Street, they make reference to that and the competition from the Government. Yet they don't go back and see that the competition from the Government in a very less inflationary time was much higher.

Mr. COBB. That's correct, sir. I've identified what I think is the problem that most economic analysts suffer under. I've called it the British neo-classical school of economics because it started with David Ricardo and John Stuart Mill, Alfred Marshall, John Maynard Keynes, and now Milton Friedman. One of the major fallacies, for example, in Keynesian analysis, is to look at a nation as if it's a closed economy, as if only the nation's own government's budget deficit and its own money supply are relevant, and that's a palpable fallacy when you recognize that in today's economy we are a one-world integrated system, especially in the capital markets.

Absolutely nothing prevents capital, liquid funds, from moving across borders and changing from one currency name to another currency name and if you try to stem it by regulations then it's smuggled across, and the point is that it is a phenomenon that we should welcome; it's a phenomenon that we should try to understand. It's a phenomenon that we cannot control through the actions of government.

Mr. NOWAK. Mr. Stoner, there's a view that holds, of course, that we should do as much as we can with the budget and even in terms of looking at the tax cut that is coming in the future and bringing some of that cut or delaying, at least, some of that cut to bring down the deficit. Do you believe that the small business community would be in favor of any kind of a delay in that personal cut, as Dr. Carlson seemed to recommend as one of the alternatives we should look at?

Mr. STONER. Yes; I heard his testimony. I guess my comment to that would be that I'm not enough of an economist myself to know whether that effect is not going to affect the high interest rates and things like inflation, and so on.

I would feel the small business community would be very happy to support the delay in the tax cuts and things that you refer to, if indeed, someone wiser than us would say that would bring a free economy with the lower inflation and lower interest rates that would go with it. If someone can make that a positive statement of fact. I suspect you would get great support.

Mr. NOWAK. Mr. Marriott?

Mr. MARRIOTT. Thank you, Mr. Chairman. I have enjoyed both of these testimonies. Let me just ask a couple of short questions.

Mr. Stoner, you indicated that, in your area of Buffalo, most of the companies who have been in business for several years are able to weather the storm of the interest rates.

Mr. STONER. Most of the companies that I'm familiar with, correct.

Mr. MARRIOTT. In other words the problem comes with the newer companies who are just getting started. Do you have any information as to whether or not the bankruptcy rate in Buffalo is a result of the interest rates or whether or not those companies have other problems that would have caused bankruptcy, independent of the interest rates? Do you have any studies on that?

Mr. STONER. No; I do not have any statistics or studies on it. The only thing that I can refer to is the one gentleman who was the head of the retailers who said that in his view most business failures were from poor management, not a single issue such as high interest.

Mr. MARRIOTT. So, your indication is that the small business argument that interest rates are devastating is more of a scapegoat than a reality?

Mr. STONER. From my view that is correct.

Mr. MARRIOTT. From your particular point of view.

Mr. STONER. I think there's something that a lot of persons, when you get into a single issue such as high interest rates, fail to realize. Small business has many, many things going for it and relative to other costs and funds, that one single cost, is certainly not the only cost to small business.

In the paper last night, I believe it was, I read that General Motors is going to start buying from outside sources rather than producing so much internally. Why? Their labor rates are $20 an hour. I guarantee you, sir, my labor rates are much less than $20 an hour, and probably in a free, competitive society will always be a lot less than the General Motors type businesses in the country.

Mr. MARRIOTT. I had a small businessman call me yesterday who's trying to get an SBA loan. Though I am no fan of SBA loans at 2½ over prime or whatever we're offering them at now, he was quite happy with the idea that he could make money at 2½ over prime and was putting all kinds of pressure on to get a $400,000 SBA loan. So that's why I'm curious about what the real impact of the interest rate is to small business, and I appreciate your input on that.

Mr. Cobb, I couldn't agree with you more on most of your analysis in terms of deregulation. I think that's absolutely necessary. The gold standard question is still a controversy in my own mind. I can argue both sides of that.

The only thing that I wonder about on your testimony is you seem to indicate that the interest rates are basically a product of marketplace phenomenon.

Mr. Cobb. Yes.

Mr. Marriott. To some extent, I agree with that; but, do you not believe the Government influences that phenomenon? For example, why is it that 5 or 6 years ago investors were willing to invest their money or loan their money at 9 percent. Today they're willing to loan it at 18 or 16 percent or whatever the money market rate might be. If nothing but the marketplace affects that scenario, why the big jump in what they're willing to invest at?

Mr. Cobb. Mr. Marriott, the Government does affect interest rates, but not by setting them. It affects interest rates in the U.S. environment by loose monetary policies, and the Federal Reserve is an agency of the Government.

Mr. Marriott. OK. I understand that, because I take the position that the Government does, in fact, send messages that affects what the interest rates are going to be.

Mr. Cobb. The Government can certainly frighten lenders.

Mr. Marriott. They have the discount rate that obviously affects something. So I was concerned that you were not implying the Government did not affect the interest rates. You were arguing that Government did not set the interest rates.

Mr. Cobb. That is correct.

Mr. Marriott. OK. I thank you, Mr. Chairman. I appreciated both of your testimonies and hope that we can get closer to some of your solutions.

Mr. Cobb. Thank you.

Mr. Nowak. Thank you very much, Mr. Marriott.

Mr. Cobb, Mr. Crane has a bill that he had put in. Are you familiar with that?

Mr. Cobb. Yes; I am. That's H.R. 3789.

Mr. Nowak. Right. Would that, in your mind, contribute to the competitiveness of the money supply system? Do you support that?

Mr. Cobb. Yes; it would. Also, Senator Symms has introduced a companion bill in the Senate, S. 1704. It's the only gold bill that is in both Houses of Congress at this time. It would affect the competitive currency environment that I alluded to in my testimony by giving the American citizen a second official U.S. currency which he could freely use, if he wanted to, and could freely refrain from using, if he wanted to refrain.

The trouble with the gold standard, as it has been advocated by journalists and other writers recently, is that it's an all-or-nothing type of thing and in the 19th century, when it was also an all-or-nothing type of thing, it did cause problems. In the 19th century it was the Bank of England in particular that was using a particular version of the gold standard to manage British capital inflows and outflows, and because Britain was the major capitalist economy in the world at that time, of course, the business cycles of Britain spilled over and caused business cycle problems in the United States and everyplace else.

The important thing about the Free Market Gold Coinage Act that Mr. Crane has introduced, is that it's a freedom-of-choice alternative. Those people that might want to make long-term loans denominated in ounces or grams of gold could do so and the interest rate that would be paid on such loans, Mr. Greenspan, former chairman of the Council of Economic Advisers, has estimated would be about 2 percent. The reason it would be so low is because the definition of what you're making your contract with would be constant. In other words, an ounce of gold today is exactly the same as an ounce of gold in the year 2000. Its purchasing power might be slightly different but we have seen through historical evidence that the purchasing power of gold is about the same today as it was in the 1830's. You can still get a good suit of men's clothes for about one ounce of gold.

The constancy of that purchasing power is what would give lenders confidence and that's why they would only ask a very small interest rate in exchange.

Now, when you're trying to make your contract in terms of dollars, unfortunately you're caught in the same dilemma that the unfortunate citizens of Oceania in George Orwell's novel, "1984," were caught into. The Ministry of Truth used to change the definitions of words. In Washington today there is an agency of the Federal Government whose principal purpose is to change the definitions of words in long-term contracts. That agency is called the Federal Reserve Board. The mere fact that it pursues something called "monetary policy," the mere fact that it's subject to a policy, tells you that it shall attempt to change the definition of the word you've just used to buy a long-term bond with.

Mr. **Nowak**. Well, thank you both very much. You've both been very informative and have brought to the attention of the committee different thoughts on this whole subject and I think we all have much food for thought as we go along in these hearings.

I would just ask that perhaps some of the members would like to ask additional questions and we're going to try to hold the record open until this is all reviewed.

Mr. **Cobb**. I would welcome written questions.

Mr. **Nowak**. Fine. Thank you very much.

Our next witnesses will be from the National Small Business Association, Carl Beck. If he'll come forward and also, because of time constraints, Wilbur S. Doyle, who is president of Doyle Lumber Co., representing the Southeastern Lumber Manufacturers Association.

Again, I understand that Mr. Weber would like to make a brief statement at this time.

Mr. **Weber**. Mr. Chairman, I understand the time constraints we're under and I do hope I can stay and listen to some more of the witnesses' testimony, but I do have some material that I'd like to submit for the record and I'd like to ask unanimous consent that I be permitted to insert some letters and material into the record of the committee.

Mr. **Nowak**. These are the letters from small businessmen?

Mr. **Weber**. Yes; from my district.

Mr. **Nowak**. Without objection, so ordered.

[See appendix, p. 149.]

Mr. **Weber**. Thank you. Mr. Chairman, if I could also ask unanimous consent that the record of these hearings be kept open for 30 days so that members can submit additional material, if that is satisfactory to do that?

Mr. **Nowak**. That would be fine. I'm just wondering if we're going to try to conclude this prior to that.

Mr. **Weber**. A more limited period of time would be acceptable as long as it's enough time.

Mr. **Nowak**. Twenty days?

Mr. **Weber**. That would be fine with me.

Mr. **Nowak**. Just in case we want to go forward with the record and I'm anticipating any movement from the administration, the Ways and Means Committee, and so forth.

Mr. **Weber**. Twenty days would be fine with me.

Mr. **Nowak**. Fine. So ordered.

Mr. **Weber**. Thank you, Mr. Chairman.

Mr. **Nowak**. We have Mr. Carl Beck, who is the president of Charles Beck Machine Corp., located in King of Prussia, Pa. Mr. Beck is the former president, I might mention, of the National Association of Small Business.

Mr. Beck, if you'd like to just withhold your testimony because of a problem that Mr. Doyle has, we'll have his testimony first and then allow him to catch an airplane very shortly.

Mr. **Beck**. Fine.

Mr. **Nowak**. Mr. Doyle is the president of Doyle Lumber Co., and chairman of the government relations committee of the association. He is also past president of the association. We welcome you once again before the committee, Mr. Doyle.

TESTIMONY OF WILBUR S. DOYLE, PRESIDENT, DOYLE LUMBER, INC.

Mr. **Doyle**. Thank you, Mr. Chairman. I appreciate this assistance in making my flight and the opportunity to appear again before you.

I am Wilbur Doyle of Doyle Lumber, Martinsville, Va., and have served or am serving, I'm not sure because we haven't been called into session this year, as a small business adviser to the Secretary of the Treasury. I am immediate past president of the legislative committee of the Small Business Council of the U.S. Chamber of Commerce. But I'm appearing here today as past president and current director of the Southeast Lumber Manufacturers, headquartered in Georgia.

SLMA, as I will call it, was founded in 1962 and is a group of small, independent lumber manufacturers who banded together for the purpose of solving industry problems. It currently has a membership of 401 small companies located in the 12 Southeastern States, making it the largest regional association of its kind in the Nation. The combined production of our mills is approximately 3 million board feet.

Mr. Chairman, to get right to the heart of the matter, record high interest rates are having a devastating effect on new housing starts, which in turn has caused a genuine depression, not a recession, in the construction, furniture, and lumber manufacturing industries. Members of SLMA, all of whom are small, independent operators, fervently believe in the free enterprise system. They are anxious and willing to do their part in helping the country get back on its feet economically.

Our problem is that it is unrealistic to ask our support of a Government long-range monetary and fiscal policy if in the interim, short term corrective measures drive us out of business. Preservation is the first law of nature, self-preservation. I might add that the weak operators, and this has been discussed here today in our business, vanished from the scene a long time ago, so I'm speaking only for the very best, efficient producers who are trying to stay alive until interest rates come back down and there is a rebound in the housing business.

To illustrate the independent lumber manufacturers' predicament, I'd like to give the committee a personal perspective. My company, Doyle Lumber, is respected within the industry as a well run, efficient operation. In each of the past 4 years the company has experienced an average sales growth of 26 percent, net per annum profits above the industry's average for the same period.

We're particularly proud of these achievements because we have witnessed a steady decline in housing through that period. The current fiscal year, which began for us May 1, we have continued to operate at 100-percent capacity, and that wasn't easy. However, finished lumber prices have dropped 25 percent while inflationary factors have continued. The good weather months, summertime for us, are historically the high water mark for housing starts. Therefore, we should have just realized our best quarter for the fiscal year. Unfortunately, we did not. Instead, we barely broke even, and I mean by barely, less than 1 percent.

New orders have fallen off sharply and we can no longer maintain the same level of production. Therefore, I anticipate that the next quarter, with these low prices and low volumes, will be the worst quarter in the 34-year history of my company.

I think that we will survive. However, had this happened to us 9 to 10 years ago when we were not a real new company but then 25 years old, I can tell you for sure we would not have survived.

Now, the entrepreneurs heading up these companies are just as hard working but they just haven't had sufficient time to build reserves necessary to sustain operations during a severe abnormal economic downturn. Further, many of SLMA's members grew substantially by using high debt to equity ratio. Unfortunately, many of these companies found it difficult to service their debt when interest rates were 12 to 14 percent. Now, with interest rates at 20, certainly it's not discretionary. You don't pay your way out of debt at 20 if you couldn't at 12. The tragedy is that many good, sound companies are going into involuntary bankruptcy.

According to a recent survey of our membership, the interest rate problem is compounded by the fact that lumber production is down 23 percent from a year earlier, with shipments declined by 28 percent. During the week of September 21 alone, SLMA members laid off 253 employees. Four companies completely shut down their operation. I should add that more of the larger producers had ceased to operate before that. They find it much easier to shuttle their people about with other plants.

But, also the small business operator has grown up close to his people and is much less willing, I think, to put this extra burden on his people if he can help it.

Since the beginning of the year, 53 companies have terminated their membership for economic reasons. Fifteen of those former members have gone out of business permanently and 10 have been acquired by very large operators who have found it an opportune time to buy out those well run companies that find themselves in a cash flow squeeze and do not have access to the capital to ride out the business cycle. The statement has been made here earlier that those bigger companies could sell for—less profit. That doesn't necessarily mean they would sell for less. They might just be less efficient. Some of these small companies are very effective and operate on a close margin.

The state of the industry which I have just described can be attributed entirely to high interest rates and the debilitating effect that that has had on the demand for lumber. There is a pentup demand. Housing would be good if interest rates were affordable. If allowed to persist, these exorbitant interest rates will cause irreparable harm to the industry and to the economy because of the tremendous roll-over effect in the economy. After all, it is the small firm that is the job generator in this country, but within SLMA I'm not aware of one single firm that's willing to expand under the current circumstances and thereby create new employment. They're afraid to.

On the contrary, many firms are contemplating closing their doors, which will create a net job loss situation. Cumulative nationwide plant closings in several industries can quickly cause a 1-percent increase in unemployment, which translates to 1 million unemployed. Now, I'm told that the Treasury translates that into $25 to $29 billion loss of revenue. So, then, high interest rates begin to feed the deficit spending and the inflation, so it becomes a part of the problem rather than a control on inflation.

While it is easy to identify high interest rates as the immediate cause of our industrywide problem, it's difficult to explain why they have stayed so high. It is even more difficult to say precisely what should be done to bring them down.

Four principal factors appear to affect interest rates: Trends in business activity, actions of the Federal Reserve Board; inflation, including expectations; and the Federal deficit. None of these factors alone, in our opinion, provide the answer, but together they begin to provide an explanation of why interest rates have remained so intransigent.

I would like to explore these different problems and offer our suggestions as to how they should be resolved.

The first issue deals with the Federal deficit. SLMA strongly supports President Reagan's successful effort to reduce Federal spending by $130 billion. We again agree with the President that further reductions in Federal spending are necessary to achieve a balanced budget in 1984. Just as importantly, the huge disparity between the revenue loss from the tax cut and the outlay reduction for the budget cut must be closed.

Congress has enacted $280 billion in tax cuts over 3 years but those cuts have only been matched by $130 billion in spending reductions. It is the administration's intent that the dynamics of the tax bill would help bridge and close that $150 billion gap, but record high interest rates have made it impossible for certain businesses to take advantage of the new incentives designed to spur additional growth and to increase productivity. Consequently, the $150 billion shortfall could represent an extremely stimulative fiscal policy which is on a collision course with the highly restrictive monetary policy. We must, I think, allow the dynamics to work.

SLMA believes that the only long-term cure for deficit spending is to adopt a constitutional amendment requiring a balanced budget. I just can't imagine you gentlemen looking your constituents in the face and turning them down on what they want and when you have the opportunity to give it to them and charge it to their grandchildren who are not there to defend themselves, so I feel that a constitutional amendment would make it easier to serve in Congress.

Second, the notion that interest rates and business activity move together makes a lot of sense and requires little explanation. One would expect interest rates, the price of funds, to be low when business financing needs are depressed and high when the needs are increasing. Yet, in the second quarter of 1981, economic activity declined and business loan demand increased by more than 9 percent.

I know that the timber industry did not contribute to that. What appears to be happening, as Senator Sam Nunn has said, is the creation of a dual economy. Certain businesses, for example, the timber industry and the automobile industry, are being crushed by high interest rates, as I said earlier, and are suffering through a depression, not a recession. Other businesses, for example, oil well drillers, defense-related industries, are experiencing a boom and have maintained a heavy demand for credit.

Further complicating the scenario is that what appears to be a desire by major corporations to furnish their needs in short-term credit markets rather than offering long-term bonds bearing 17-percent interest. Certainly these companies cannot be blamed for making sound business decisions, but it is a fact.

Third, an increased demand for credit must be juxtaposed with the tight monetary policy of the Federal Reserve. While we appreciate rapid growth in the monetary supply creates real inflation, and fuels inflationary expectations, we nevertheless believe that the Fed can bring our monetary growth in line with its projected target for M1-B of between 3½ and 6 percent.

During the first 8 months of this year, the money supply of M1-B actually grew at about 2 percent. In our opinion there is simply no reason for overkill by coming under the goals established by the Fed. Obviously, a modest increase in money supply could bring some immediate short-term relief to the smaller businesses who are prolific job creators.

In addition to the passage of a balanced budget amendment and action by the Federal Reserve, SLMA believes there are fiscal policy options available to the Congress. We believe that the administration would help avoid a further clash between fiscal and monetary policies. Each point would serve to reduce additional Government borrowing in the next few months and thereby help eliminate the extreme pressure on interest rates.

Defense spending should be scrutinized more closely. A fairly rapid buildup of our defense system is likely to cause tremendous waste and inefficiency unless the Defense Department is held strictly accountable. More prudent, measured growth of our defense capability may be in order rather than added deficit spending which will indirectly weaken our national economy. We recognize that without a strong national defense all could be lost, but in the interim the will to use our existing defense arsenal should serve as an effective deterrent.

Third, other areas of the budget can and should be cut. Modification of entitlement spending coupled with a leaner defense budget should serve to make the job of the President easier.

Finally, Mr. Chairman, the time has come for people in leadership positions to realize that small business is bearing an inordinate burden in helping to redress our economic woes. The small business person is perfectly willing to assume his share of the responsibility, but it is unreasonable and unrealistic to ask him to support long-range goals, regardless of how good they are, if the short-term solutions cause him bankruptcy.

I wrote Senator Byrd recently and told him that when I go to the vet, to pick up a pill for my dog, the first thing the vet wants to know is how big your dog is. He knows that the right medicine in the wrong size will kill a healthy puppy, and we're getting it. This means interest rates must come down to realistic levels. Further, the very essence of supply side economics is increased productivity, but it cannot work with exorbitant interest rates smothering the ability of the entrepreneur to make new investments. Congress and the administration must work together to develop mutually reinforcing fiscal and monetary policies to guarantee not only the survival, but the contribution. of the entrepreneur. The longer the day of reckoning takes, the greater the harm to the economy and your constituents.

And I thank you very much for the opportunity to appear.

Mr. NOWAK. Thank you very much, Mr. Doyle. The witness prior to you, Mr. Cobb, was talking about the deficit also and had some very different types of recommendations as to what we can do. In looking at the chart, it indicates the year 1958 when the publicly held national debt as a percentage of the gross national product was 51.6 percent. Today the publicly held national debt as a percentage of gross national product is much lower, and yet the interest rate in 1958 or the inflation rate in 1958 was under much greater control, despite the tremendous debt that the country was carrying. I've wondered about this too because it's in inverse relationship to what the traditional thinking has been and, of course, especially the Wall Street mentality concerning this has been. The budget cuts notwithstanding, as some of the other witnesses have testified, would you favor a postponement or some delay in the tax cut to arrive at that balanced budget position?

Mr. DOYLE. Mr. Nowak, I think anything that helps people live through this crucial period, from my people's point of view, would be desirable. The only thing that concerns me about that is that the budget cuts, as they were finally made, where the small corporations such as mine wound up receiving the 1 percent a year for 2 years, were of no great consequence, frankly, to what we're doing. We got the capital cost recovery bill through, but again, the benefit, the predominant benefit, is to the capital intensive industry.

We don't need more benefits right now. We need profit. We can't take advantage of the funds that we've already got available if we can't make a profit. It seems to me to say, "Would you be willing to take these cuts?" About the only benefit many small, unincorporated businesses get out of this tax bill, one of the major ones, was the tax cut. To take it away from them is asking them to bear still more of the burden. I think they're willing to do whatever is equitable, but what concerns me is, look at the figures that went in to capital cost recovery, where that went. Look at the $9 billion that went to the oil drilling and so on. So, before you take about the only thing they've got away to balance the budget, it seems to me that some redress is far more equitable than that.

Mr. **Nowak**. It has also been a suggestion at least, as a thought by the administration or at least by some people in the administration, to look at housing in a little different light than we have in the past. We talked about this American dream, or as somebody had called it recently, the American tragedy, in trying to stimulate housing. They saw it as more of a speculation, to some degree, and in fact the suggestion was made that perhaps the Congress would like to look at the interest deduction that is now in place and either remove the interest deduction on a home mortgage, or in the alternative, limit that interest to some particular amount of money, which again would be a deterrent to home building or private ownership in the very least.

I'm just wondering unless there is some specific action taken, and this scenario just plays out the way it is, if we're not going to severely limit first of all, the new homeowners and second, of course, the people who would have liked to have upgraded into another house? Will we create a rental situation as the Europeans have done in vastly greater numbers, where that becomes an investment for the owner, the landlord, so to speak, and we spread out the new owners as tenants rather than owners.

Do you have any feeling for this?

Mr. **Doyle**. Well, I think there is a social implication in owning a home. I think it stabilizes families and I think it gives them pride and it gives them something to work on that they can call their own and I believe that from that point of view it is good.

I would point out one of the things that makes it very difficult to build homes, again, is regulation. I was here in a meeting a few years ago and we wanted to build cheap houses. Well, time is valuable but let me tell you a quick story. In my business we buy old farms. We need to grow timber and we're looking for land. We bought one and there was a house on it, three rooms, a man living in the house. He came and wanted and know if we were going to rent the house and I said, "No, I'm not going to do anything with it." He said, "Can I stay?" and I said "So long as you don't ask us for anything, stay. No problem. We're not going to do anything for it and you're not going to pay us." This man stayed there and raised seven children in a three-room house with an outside john and a spring 100 yards away.

A few years later he was given the opportunity not to go in debt a little bit, but to build a house, and he arranged the financing and they found that instead of being seven in the family in all, that he had seven children instead, so after the house was completed, with 2½ baths and so many bedrooms, he was told: no, we've made a mistake. You can't move in that house until another bath is built, since it doesn't meet the standards.

We have set the standards so terribly high, we don't allow anybody to start out. It used to be you could build two rooms and build onto it, build a basement, put a roof on it, and move in it. But now we're not satisfied until we force people into debt beyond what they're able to carry. So, I think the area that we need to look at, from that point of view, is get some of the regulations out of these programs and let people use some common sense and do what they can afford and crawl before they run.

Mr. NOWAK. I think your suggestion in your testimony about looking at both sides of the picture is important. The defense area, I think, is one that is being scrutinized right now to further reduce the total outlays by the Government. I just have to feel that that will be one area where perhaps the President's recommendation will be exceeded, once Congress gets into the specifics and hopefully that pressure will start to subside to some degree.

But I just think we're in for an awful long period of time if nothing is done and no focus is given to this interest rate problem. It's been said many times that it's the symptom of the disease and so forth, but unless there is some focus on that, I'm just afraid in the period of another 6 months or a year you're going to see an awful lot of harm, irreparable harm, done to the small business community that is just unable to cope with this over that kind of a timeframe. I wonder about the free enterprise system in Japan and how they're able to allocate credit governmentally to certain industries to produce and to almost subsidize those interest rates through their banking system and why they're having so much success in competing on the world markets in those six or seven areas. That will be a question that I think should be answered.

As I view it, you're going to have some super companies growing up in certain areas and like the A.T. & T. situation, you have everybody wanting deregulation, but the competitors of A.T. & T. want some restrictions on that regulation. As they envision it complete deregulation would mean the establishment of one A.T. & T. network totally and completely to the exclusion of everybody else because of their strong market position. I don't know how many other industries that may happen to, but we want to thank you for your testimony.

Mr. DOYLE. I might say one thing, sir. I met recently, to show you the difference in these two situations, with the vice president of one of the major companies in my industry. His company allocated $100 million for the purchase of land and raw material this year. I met with another one who said that we were able to maintain our profits this year because of cash coming out of Government confiscated redwood lands, you see.

So, again, I can produce cheaper than those companies, more economically than they can, and thus the consumer is better off, but I'd hate to leave here with anybody feeling that the companies that are going down now are bad operations. They aren't. They're people with 20 or 25 years, maybe, good operators. They simply have been in this so long that they have run out of reserves to operate and it is an emergency situation.

Mr. Nowak. Mr. Centner.

Mr. Centner. Mr. Doyle, Mr. Marriott has proposed a small business participating loan. Are you familiar with that?

Mr. Doyle. Yes, sir.

Mr. Centner. Would the ability to negotiate an interest rate in the marketplace be of assistance during a high interest period like this for a small business like yours?

Mr. Doyle. I gave that to our accountant and asked him to look at it and his statement was that probably it would be very slow to operate, in the first place, if it brings other people in and the average small business doesn't have in place the types of things that the SEC is looking for. It gets this thing complicated. He felt that it would be generally more expensive than the small business could negotiate, particularly if he's in a small community with a small-town bank.

Mr. Centner. First of all, the bill explicitly excludes the SEC from regulating it. The other thing is that we've added to the bill, as it was proposed in the past, a tax credit of 20 percent or $20,000 for the lender or 30 percent or $30,000 if he loans the money to a minority or disadvantaged business; in other words, we're sweetening the pot for the lender. Would that sort of a situation improve it, do you think?

Mr. Doyle. I think it could help. I met with the president of our bank yesterday, talking about it. The nonproductive sector of the economy is their best market for funds, so as things mature, what they're doing just as fast as they can, they turn them over. What I don't understand, why is Treasury going so far out? Now, at these high interest rates, they're turning them into long-term 4- and 5-year 16½, 17 percent locked in interest rates. Why fool with us if you can do that? That's one of our problems. Get them out from the front of the borrowing line and we can make it competing with the private sector that has to make a profit off of the money, but we can't compete with them when there's no limit to what they can get.

Mr. Nowak. Thank you very much, and we'll again may have further questions and we'll be able to get in touch with you.

Mr. Doyle. Thank you, sir.

Mr. Nowak. Thank you, Mr. Doyle.

Mr. Doyle. May I be excused to catch that plane?

Mr. Nowak. Go right ahead. You've got 8 minutes.

Mr. Beck, thank you for your patience and once again I just want to repeat that Mr. Beck is a former president of the National Small Business Association and we want to welcome you before the subcommittee. He's accompanied by Herb Spira, who is the tax counsel of the NSBA.

Mr. Beck. Thank you, Mr. Chairman. Yes, I am Carl A. Beck of Charles Beck Machine Corp. I'd like to submit my prepared statement for the record and just offer some comments.

Mr. Nowak. Without objection, so ordered.

[Mr. Beck's prepared statement follows:]

PREPARED STATEMENT OF CARL A. BECK, ON BEHALF OF THE NATIONAL SMALL BUSINESS ASSOCIATION

Good Morning Mr. Chairman and distinguished members of the Subcommittee:

My name is Carl Beck, President of Chas. Beck Machine Corp. of King of Prussia, Pennsylvania. I am a former President of the National Small Business Association (NSB). With me is Jerome Gulan, Vice President, Government Affairs of NSB, and Herbert Spira, Tax Counsel of the National Small Business Association.

The National Small Business Association, founded in 1937 as a multi-industry trade association, represents more than 50,000 small businesses nationwide.

REVIEW OF PRIOR RECOMMENDATIONS

When I appeared before this Subcommittee last March 25th, our testimony applauded the position of both the President and the Congress that the top priority was to reduce inflation, increase productivity, and improve the basic foundations of our national economy. We commended the Reagan Administration for emphasizing the interdependence of budget, tax, and monetary policies in order to reach these vital objectives.

The fourteen million small buinesses which account for 48 percent of the domestic output of our economy are, in turn, dependent for their profitability -- and their survival -- upon the success of these policies.

Our testimony made a series of recommendations on the basis of concerns expressed by leading economists and it is relevant to review them at this time:

° We urged that information on the impact of the proposed tax cuts, by industry and business size (particularly as to small business) be developed and analyzed before action on the bill. To our knowledge, a study of the prospective effects of the bill on small business has yet to emerge;

° We recommended consideration of holding down the overall size of tax reductions "within limits that will preserve a cushion for responsible fiscal policy and hopefully budget balance over the near term." Our statement pointed out that the revenue losses predicted through fiscal years 1986 were $554 billion for individual tax reductions and $164.3 billion for business tax cuts, or a total of $718.3 billion in revenues foregone, with an off-set of $15.0 billion in proposed new charges.

° It was our hope that the proportion of the revenues devoted to business capital formation be increased from the proposed 23 percent to 45 or 50 percent to build up the supply side of the economy.

° We proposed that the form of the tax reductions be designed for maximum anti-inflationary impact, such as targeting reductions to savings and investment, targeting to the dynamic small business segment of the economy and targeting to Social Security offsets, which would directly affect the cost of labor in all goods and services.

The tax bill, as finally enacted, amounted to $748.8 billion through fiscal year 1986, even larger than the original proposal, and with a prospect of even more sizable revenue losses after 1986 because indexing of personal income taxes and the full 200 percent declining balance depreciation becomes effective in that year.

INTEREST RATES HANG HIGH

Interest rates, which are shaped by the total economic picture, including climate conditions, worldwide and domestic political, social, and business factors as well as tax, budget and monetary policies, are at the highest levels since the Civil War.

Short-term rates, as represented by the "prime rate" peaked at 21 1/2 percent in 1980 and at 20 1/2 percent already in 1981.

Although there has been a welcome reduction in recent weeks, the startling levels of current interest rates compared to traditional levels is summarized in the following table:

HIGH CURRENT INTEREST RATES

1981 compared to 1976

	Sept. 20, 1981	Average 1976
3-month Treasury bills	14.198	4.989
3-year Treasury rates	15.980	6.770
10-year Treasury bonds	15.21	7.61
High Grade Municipal bonds (Standard & Poor's Index)	12.47	6.49
Corporate AAA bonds (Moody's)	15.35	8.43
Prime 6-month Commercial paper	15.29	5.35
Federal Reserve Discount Rate	14.0	5.50
Prime Rate	20-19 1/2	6.84
New Home Mortgages (August 1981)	15.27	8.99

SMALL BUSINESSES ARE HURT FIRST AND HARDEST

It is almost universally recognized that small businesses bear the greatest burden of any credit squeeze.

Council of Economic Adviser's Chairman Murray Weidenbaum told the Wall Street Journal:

> "In periods of monetary restraint, the smaller, weaker borrowers suffer most." 1/

In an attempt to measure the financial impact of high rates in detail, our association recently completed a report on business bankruptcies. 2/

1/ "Surge in Interest Rates Puts Squeeze on Already Ailing Economic Sectors," by Tom Herman and Edward P. Foldessy; May 7, 1981; first page of second section; page 29.

2/ "Report on Business Bankruptcies," National Small Business Association, September 21, 1981.

BANKRUPTCIES

We found a dramatic rise in business failures that has been parallel to interest rate movements. From mid-1980 to mid-1981, business bankruptcies tabulated by the U.S. Courts increased 30.1 percent over the previous year. That is the second largest year-to-year rise of the past 20 years, exceeded by only the 45.2 percent increase occurring between 1974 and 1975. 3/ Court-filed bankruptcies have thus been running at an all-time record rate of more than 4,000 per month since January, 1981.

Even more current and more alarming are figures from Dun & Bradstreet for January 1 through September 3, 1981, which reflect that business bankruptcies increased from 7812 to 11,076, a jump of 41.8 percent compared with the same 35 week period in 1980. 4/

Smaller businesses (defined as those with liabilities of $100,000 or less) comprised 50.53 percent of the 1981 total, and reportedly businesses with $1 million or less accounted for about 90 percent.

It is also well known that certain industries are particularly sensitive to interest rates, and have therefore taken a beating from high rates. These include home building, construction, automobile and farm implements. 5/

3/ Court filings are on the basis of the "statistical year" of the U.S. Courts which record the information. For the past two years the figures have been as follows:

Statistical Year July 1, 1979 - June 30, 1980 = 36,433
Statistical Year July 1, 1980 - June 30, 1981 = 47,414 *

*Excluding joint petitions.

4/ "Business Failures Increase," *New York Times*, September 13, 1981.

5/ Herman and Foldessy; op. cit.

An industry breakdown of the D&B figures for the 35-week period is as follows:

1981 Compared to 1980	
Construction	up 48.5%
Services	up 37.6%
Retailing	up 41.4%
Manufacturing	up 36.9%
Wholesaling	up 30.1%

Since many small businesses are under-capitalized to begin with, owners are often required to put up personal assets such as their homes as additional security for business loans. If a bankruptcy follows, an owner can also have his family life shattered, exacting a "toll of personal tragedy." 6/

We must also emphasize to this Subcommittee the many reports of well-managed, hitherto sound businesses which are at the end of their rope, and which will not be able to continue in the face of persistent rates in the neighborhood of 20 percent. 7/

IMPACT OF INTEREST RATES ON SMALL BUSINESS CAPITAL FORMATION AND SURVIVAL

In the best of times, capital formation is more difficult for smaller firms than for larger ones.

A fresh study by the Reagan Administration clearly establishes anew the disadvantage of smaller size.

The Commerce Department utilized five banks in various regions across the country to take samples of the business community and survey the unmet needs for capital. 8/

6/ Interviews with Samuel Greenbaum, Esq. and Charles A. Doctor, Esq., Washington, D.C., September-October, 1981.

7/ See Testimony of William D. Barth, Director of Small Business Practice, Arthur Andersen & Co. before the Senate Finance Committee in behalf of NSB's Small Business Legislative Council, May 20, 1981.

8/ "An Empirical Analysis of Unmet Demands in Domestic Capital Markets in five U.S. Regions," U.S. Department of Commerce, February, 1981.

This study concluded:

- Capital gaps are a reality (page 4);
- Gaps as to borrowed funds occur primarily in the intermediate to long-term maturities (page 4);
- Independent firms are at a disadvantage in capital markets (page 5); and
- Small firms have the most difficulty obtaining capital (page 5).

In the area of equity capital, hearings in the Senate have documented similar difficulties of smaller and even medium-sized businesses, especially at the bottom of difficult economic cycles. 9/

These problems are dramatized by the statistics for the mid-1970s, which show that small firms (worth $5 million or less) were able to sell only nine registered stock issues in 1974 and four in 1975. 10/

WHAT CAN BE DONE?

Our association has attempted to identify avenues of relief.

We find at least four areas worth pursuing -- representation, improvement of data, general economic policy, and possible specific creative interim small business financing techniques.

Representation

NSB believes that providing access for the small business view point to major governmental and private economic decision-making is an essential beginning.

Accordingly, NSB favors such measures as the representation of small business experience on the Federal Reserve Board and at the upper reaches of the Executive branch by means of a Small Business Advisory Council (or Councils) and small

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9/ See 31st Annual Report, Senate Small Business Committee, Chapter III, pp. 29-62.

10/ 31st Annual Report, loc. cit, page 34.

business representation on, or monitoring of, two of the five Cabinet Councils: Economic Affairs, and Trade & Commerce.

Data

Once access is obtained, the input should be of the highest quality. NSB therefore favors improved small business financial data as a basis for decisions, and a strengthened advocacy function to develop and present this information.

NSB is working with a number of leading economists and organizations to develop a series of small business indicators which can reflect the financial health and needs of small firms on a continuing basis.

General Economic Policy

It is the opinion of NSB that the closer we can come to a balanced budget, the better off small business will be.

This involves the broadest of fiscal and monetary considerations.

NSB, however, is disturbed by reports that a budget strategy might be needed to cope with deficits of as much as $50 to $100 billion in 1983 and 1984 11/ and up to $200 billion in the latter half of the decade. 12/

We believe that our system is not built to operate under sustained high interest costs which would be likely to accompany such possibilities, and small business would be the first but not the only casualty of such a scenario.

We therefore recommend, as an urgent matter, that Congress and the Administration make every effort to arrive at agreed upon economic assumptions, and to decide as soon as possible at the tax, spending, and monetary policies that assure that the nation is on the path to fiscal responsibility and a balanced budget.

11/ "Needed: A Budget Strategy," Editorial, Washington Post, October 9, 1981, page A-30:1. Also see "Reagan's Balanced Budget -- one step closer, one step further away" National Journal, Sept. 26, 1981, pg. 1712.

12/ Testimony before the Senate Small Business Committee on Interest Rates and Business Credit Needs, September 23, 1981.

Such agreement is crucial to small business, as any period of uncertainty would be an additional spur to keeping rates high.

Credit crunches resulting from high interest rates do not restrict the public sector. The federal government obtains all the money it needs at whatever price it must pay.

High rates are not inhibiting our greatest corporations from purchasing other corporations. 13/

Large companies have many options for raising necessary funds that smaller firms do not - commercial paper, Euro-loans, multiple lines of credit, assets to borrow against, and established internal cash flow.

High interest rates mean that small business bears the brunt of economic re-adjustment.

Creative Financing

Small business has much to gain from economic stabilization with its accompanying lower inflation and lower interest rates.

Therefore, small business has been willing to absorb its share -- and probably more than its share -- of the bitter medicine of economic slow down.

However, if the price of national success is the failure of thousands of sound and well-managed small firms, that is a dreadful price to pay.

We think it is unconscionable for the government to allow such firms to go under in record numbers without offering some life-line.

What we need is a fresh approach to tiding over small business in this period of brutal credit stringency. It is essential for our economy that we explore every possible way of relieving pressure on our small businesses.

13/ "Sears Makes Bid to Buy Dean Witter Reynolds" by James L. Rowe, Jr., Washington Post, October 9, 1981 page D8:1. The article recites that Sears also announced on October 5 that it will purchase the biggest independent real estate company for $179 million. Other recent transactions reviewed include Prudential Insurance's purchase of Bache, the American Express acquisition of Shearson Loeb Rhoades, and Phibro Corporation's purchase of Salomon Brothers. The Conoco-Dupont merger also took place in 1981.

If government feels it must cut back the guarantee loan and special bond-financing programs which were conceived specifically to weather difficult economic times, it should at least offer some stop-gap alternatives.

Our association has attempted to put together several possible creative financing methods which we proposed to investigate with the Administration and now propose to explore with the Congress.

These include:

- Mutual guaranties and/or mutual lending between small firms;
- The possibility of allowing small firms to borrow from pension funds, with adequate security, particularly under the leasing provisions of the new tax law;
- Permitting equity banking for small enterprise through private financial institutions;
- The speed-up of payments to small firms on government contracts perhaps through a revolving fund;
- Possible temporary reinstitution of the banking system's discount window for special use funds or targeted credit allocations;
- Imaginative tax strategies such as reinstituting the cost-effective general jobs credit and establishment of new financial instruments, such as the small business participating debenture; and
- Pursuing the capital formation possibilities spelled out in last year's Securities Act Ammendments.

These methods share the characteristics of costing the government little or no money. They would operate by removing barriers to the investments of capital in small or other business.

SUMMARY

We feel that the small business is the prime victim of the prime rate. Reduced capital costs is the number one need of American small business, which can not survive otherwise.

Approaches of the kind described above are absolutely essential if small business is not to bear a heavily disproportionate share of the national sacrifices for economic revitalization.

# # #

TESTIMONY OF CARL A. BECK, CHARLES BECK MACHINE CORP., ON BEHALF OF NATIONAL SMALL BUSINESS ASSOCIATION, ACCOMPANIED BY HERBERT SPIRA, TAX COUNSEL

Mr. BECK. Thank you, sir.

In our testimony, I hope you will be aware of the fact that we are not recommending the Fed ease money control and interest rates. I think, as people have demonstrated in the last couple of years quite well, the Federal rate is the result of, not the cause of, the rate, and we have been going with easy money for too many years. Our problem is inflation in the long run.

There are certainly many things that contribute to the problem we're discussing today, high interest rates, and the concomitant shortage of capital for small business. But, we can't say that the Federal discount rate or its actions on the open market committee really are a significant part of it, although, of course, they contribute. Certainly, the Federal budget deficit contributes. It doesn't set the rates but it certainly contributes.

But most important, I think, is the uncertainty. We see it in our customers, a reluctance to buy machinery which they have committed themselves, eventually, to purchase, and they keep pushing it off because of the signals that are coming from the Federal Government, whether it be Congress or the administration. The signals are confused. The Fed, at least, if you can believe most of what you hear is at least being consistent.

You recall back on March 25, when I appeared before you we discussed the problem of the initial proposals for tax reduction and their cost to the Government and we had very serious concerns about the amount of the tax cuts and many suggestions, as to ways that certain results could be accomplished without the high drain of reduction of tax income to the Federal Government.

Of course, with your help, thank you, sir, and many of us speaking the same language, you certainly did have some effect on the Ways and Means Committee on that. But, still the tax cut was much higher than I think many of us felt was proper, and this certainly is contributing to the increased or increasing or continuing, as you might want to define it, Federal deficit.

We certainly agree with what has been said here today by so many people that there's got to be a real control of Federal expenditures and as citizens sitting on the outside, we feel that there's an awful lot more that Congress and the administration can do in reducing Federal expenditures.

But, as I said earlier, the problem is inflation and curing inflation and if we didn't have the inflation and the uncertainty about the clouded crystal ball of what it's going to be in the future, we wouldn't have the high interest rates we have today. Let's put the tag on the donkey where it belongs. That is the problem and we have offered, in our testimony, some suggestions as to things that might be explored, none of them, admittedly, near term. Some of them have to do with the administration and with reforming certain regulations. Some of them perhaps require congressional activity. These we have already begun investigating with certain people in the Treasury Department and the administration and we hope that we might further investigate these and work with Congress and particularly this committee.

On page 9 we've listed these very briefly and we talk about mutual guarantees or mutual lending between small firms, something that's going on very well in France today and hasn't really been thought of here. Perhaps it would be innovative in our economy but there are certain regulatory things that prevent it.

The second one is the possibility of allowing small firms to borrow from pensions funds. We know the IRS is permitting this on a case-by-case basis but it ought to be more readily available because it is a source of capital which today, as you know, goes into the market and the pension funds of the small business go into the market to support the big companies and the big companies' stock purchases and so on.

A third one, equity banking for a small enterprise through private financial institutions. The banks are quite restricted by regulations today as to what they can do and at the moment proposed banking deregulation doesn't seem to hit on this as well as it should.

The fourth one was the speed up of payments to small firms on Government contracts. In dealing with our suppliers, when we don't pay our bills, we pay a penalty, and we get a discount if we pay them, maybe 2 percent in 10 days, but the Federal Government says to small business, That's your problem. If we want to be 3 months late in our payment, that's up to us. That isn't quite fair either. If there's something that we can do to encourage the Government to pay its bills promptly and regularly, like business pays its bills, it would certainly help the flow of funds to small business, who are hurt most by that.

Another thing we've mentioned is possible temporary restitution of the discount window for special funds. This was tried for a limited period. I don't know how successful it is adjudged to be in hindsight, but it did seem at the time it was of some help.

Then I've also mentioned imaginative tax strategies such as reinstituting a cost-effective general jobs tax credit. We've always known that the small business sector creates the new jobs or 90 percent of them, and if we want to get the economy moving again, this might be a way that we should revert to instead of just the targeted credits we've been living with on a very limited basis for the last couple of years.

The last recommendation had to do with the last year's Security Act amendments. There were supposed to be two conferences on capital formation annually, one for State people and the other one having to do with small business. I think this is an area, if this could be encouraged to get moving, where many of the things that we're talking about here might be able to be investigated with small business participation and input in such a conference he could look at some of these problems to see what innovative ways might be developed to overcome this problem that we have today. Again may I underline that we are talking about no additional Federal expenditures and we are not talking about a lot of special breaks and we are not talking about budget busting or any more Federal funds, but things that can be done purely with some regulatory reform and perhaps, in some cases, some congressional easing of the rules.

I think that's the essence of what we're proposing and we are, naturally, available, as we've been in the past, if there's any way we can help to investigate these things further. We do have an active campaign of investigating these things to see what can be done.

Mr. NOWAK. Thank you very much, Mr. Beck. You had, I understand, some contact with members of the Federal Reserve Board as well as people in the executive branch concerning some of these proposals. Is that correct?

Mr. BECK. We have been talking mainly with the Treasury, I believe, and the Council of Economic Advisers. We have talked to them and discussed some of these things with them. I don't think we've been in touch with the Fed, particularly; no.

Mr. NOWAK. How have the ideas been received by them? Have you any kind of a response back to any of the points?

Mr. BECK. I would say that basically they felt they are somewhat innovative. Maybe Mr. Spira could answer this more correctly.

Mr. SPIRA. We received an invitation to pursue the pension matters with Dr. Niskanen of the Council of Economic Advisers and, as to the other financial matters, it was suggested that we go over to Treasury and present them to Assistant Secretary Mailey.

Mr. NOWAK. You haven't done that yet, Mr. Spira?

Mr. SPIRA. We are going to soon.

Mr. NOWAK. You are going to do that. OK.

The second or third one you mention here, equity banking for small enterprises, could you give me some detail as to how you implement that?

Mr. BECK. It's done in Holland quite a bit, I understand, and I'm not familiar with the details. Essentially what we're talking about is something different from a small business investment company of a bank, but rather, an opportunity for a bank to make money available secured not by a piece of equipment, but by stock of the company, which can be bought back by the borrower of funds or the seller, temporary seller, of the stock of the small business, at sometime in the future at a fixed markup over a current price and so on.

Mr. NOWAK. You'd collateralize the loan, then, by an issuance of stock?

Mr. BECK. Or by sale of current shares of stock of the company to collateralize the loan with concomitant ownership, partial ownership of the business and so on, stock which then is repurchasable by the individual.

It is a way that under today's laws, of course, just isn't permitted.

Mr. NOWAK. I think you've got some good ideas to pursue here, and I would be happy to hear what the Treasury, Herb, would say when your discussions get down to some detail. I just foresee a continuation of the type of rates we've had recently, unless there is some other way to finance some of this expansion. As other witnesses have testified, it may not put everybody out of business but it certainly is going to prevent a lot of innovation and a lot of expansion at these kinds of rates because the alternative, of course, is to just take your 17 or 18 percent in the money market and forget about the risk until these rates somehow come down, if they ever do, in the future. You can just be postponing an awful lot of productive investment and be counterproductive to what the administration is really trying to do with the economy.

Mr. BECK. I'm glad you mentioned that, sir, because I think today the high interest rates in many cases aren't just a problem of high interest rate or the interest cost but an opportunity cost. In our business, for example, we have two major research and development programs underway in terms of new designs of machinery and one of those is pretty much in-house and the other one required investment of a considerable number of components, at some expense. We have, because of the current business situation, just cut the second one out temporarily. We've delayed it and it may be another year or so before we get back to it.

So, it's really lost opportunity costs in many cases, although I'm sure in the homebuilding it's much more direct than, for example, it is in our business.

Mr. NOWAK. Fine. Well, let me once again congratulate your organization for pursuing all of these different alternatives and we'll be looking forward to any further information that is gathered.

Mr. BECK. If you'd like to have it, I'll be glad to submit, for the record, our report on business bankruptcy dated September 21, 1981, which we've just brought here.

Mr. NOWAK. We appreciate that and that'll be made part of the total record.

Mr. BECK. Fine.

Mr. NOWAK. Thank you very much for your association's participation.

[Material referred to above follows:]

REPORT ON BUSINESS BANKRUPTCIES

Prepared by National Small Business Association -- September 21, 1981

Business Failures: Current Statistics

From mid-1980 to mid-1981 court-filed business bankruptcies increased 30.1 percent. This is the second largest year-to-year rise of the past 20 years, below only the 45.2 percent increase occurring between 1974 and 1975.

Even more alarming are more current figures from Dun & Bradstreet for January 1 through September 3, 1981, which reflect that business bankruptcies increased from 7,812 to 11,076, a jump of 41.8 percent compared with the same 35 week period in 1980, according to press reports quoting Rowena Wyant, a D&B Vice President in the New York business economics division ("Business Failures Increase," New York Times, September 13, 1981.)

Smaller businesses (defined as those with liabilities of $100,000 or less) comprised 50.53 percent of the 1981 total.

An industry breakdown of the D&B figures for the 35-week period is as follows:

1981 Compared to 1980

Construction	up 48.5%
Services	up 47.6%
Retailing	up 41.4%
Manufacturing	up 36.9%
Wholesaling	up 30.1%

This information is probably conservative from the small firm standpoint, because D&B figures do not include the finance, insurance, and real estate fields where smaller businesses predominate.

In a recent newspaper column George Will characterized similar figures as "a massacre on Main Street." (The Massacre on Main Street," Washington Post, September 20, 1981, page C8:1)

The court filings are on the basis of the "statistical year" of the U.S. Courts which record the information, which for the past two years has been as follows:

Statistical Year July 1, 1979 - June 30, 1980 = 36,433
Statistical Year July 1, 1980 - June 30, 1981 = 47,414

Notes

As a technical matter, it should be noted that courts also accept Joint Petitions. These are additional filings where the husband and wife both participate in the enterprise. These are excluded from the above figures, because a "joint petition" covers persons associated with a business that has already filed. Inclusion of joint petitions would increase the business total for the 1980-81 statistical year to 66,000.

The statistics are also affected by changes in the bankruptcy laws brought about by the Bankruptcy Reform Act of 1978 (effective October 1, 1979). The new code did not make it easier for corporations to file. The law did establish a series of personal exemptions in federal law for the first time which, in many instances, were more liberal than state laws. (Bankruptcy Code, Sec. 522). However, there were not and are not any corporate exemptions, and corporations can no longer be discharged of debt as they could under the old law.

Historical Trends

The statistics on bankruptcies since 1950, as collected by both the U.S. Courts and Dun & Bradstreet are set forth in a chronological table attached as Exhibit 1.

The data show that business bankruptcies have risen and fallen in cycles. From mid-1961 through mid-1970, court-filed bankruptcies by businesses held almost constant (averaging about 16,200 per year, or 1350 per month). Then from mid-1971 to mid-1976, the figure more than doubled to 35,201 (about 2900 per month). Thereafter, the level declined until the end of 1979, when it stabilized at about 2,500 per month, as shown in the following table:

Court filed bankruptcies mid-1975 to mid-1979

1975-76	35,201
1976-77	32,189
1977-78	30,528
1978-79	29,500

Within a few months after the Federal Reserve action of October 1979 boosted interest rates to then-record levels, business bankruptcies began to climb dramatically. Totals reached an average of about 3,800 per month in the spring of 1980, where they remained until this year (1981) when they hit a new plateau of about 4,000 per month. This can be seen in the following quarterly tabulations:

	July-September	October-December	January-March	April-June
Statistical Year 1980-81	11,674 ('80)	11,227 ('80)	12,101 ('81)	12,081 ('81)
Statistical Year 1979-80	8,457 ('79)	7,014 ('79)	9,137 ('80)	11,473 ('80)

Thus, the business bankruptcy level increased 63.57 percent from the beginning of October, 1979 to the end of June, 1980.

Particularly Hard-Hit Industries

Some industries are particularly hard hit, such as construction. According to Dun & Bradstreet, bankruptcy rates for building contractors and subcontractors increased 48.5 percent through September 3, 1981 over the same period in 1980 (by which time the casualty figures had already risen substantially from the 1979 lows.)

A break-out of comparable figures for the first three months of this year shows:

Failure in Building and Construction

	January-February-March 1981	January-February-March 1980	Increase #	%
General Building Contractors	282	228	54	23.68
Building Subcontractors	358	218	140	64.22
Other Contractors	45	22	23	104.55
	685	463	222	47.95

Source: Dun & Bradstreet, New York.

In automobile distribution, 1650 new car dealers went out of business in 1980, the largest total ever. Another 325 have failed during the first 6 months of 1981, bringing the overall exodus close to 9 percent of all businesses in this field since 1979 (NADA Data for 1981, National Association of Automobile Dealers).

"Walkaways"

There are also innumerable instances when businesses just close their doors and terminate the business. They may now owe creditors nothing. Or, they may have substantial debts which are satisfied through attachments on bank accounts or foreclosing tax liens or mortgages, leaving few assets for general creditors to pursue in any kind of formal proceeding. There is probably no overall source of statistics on these "walkaways," but experts believe the number is substantial.

Relationship Between Individual Bankruptcies and Business Bankruptcies

Court-filed bankruptcy rates for individuals have more than doubled since the new bankruptcy code became effective in October 1979:

Non-Business Bankruptcies

1978-79	196,976
1979-80	314,856
1980-81	450,000 (preliminary)

These personal bankruptcies have direct ramifications for small business.

When an individual declares bankruptcy, the creditors are left "holding the bag," which is almost always empty.

Prominent among these creditors are the retailers, distributors, builders and service enterprises where the bankrupt ran up the bills which caused the problems. Many of these are small business.

For example, the May Company reported 1980 losses increasing 103.3 percent to $3.6 million compared to 1979. For J.C. Penney, losses increased 102 percent to $20.7 million. Montgomery Ward's losses increased 117 percent to $50.6 million, while Sears' losses increased 120.4 percent to $46.2 million for the same period.

Local businesses have the same kind of trouble. In fact, some of the regional independent stores, which are members of the National Retail Merchants Association, reported 1980 losses increasing over 200 percent compared to 1979.

Relationship Between Interest Rates and Bankruptcies

These cycles raise the question of how interest rates affect bankruptcies. As can be seen from comparing interest rate movements with the bankruptcy cycles documented by Dun & Bradstreet and the U.S. Courts, bankruptcies have tracked the interest rate very closely in recent years. This is illustrated by the chart attached as Exhibit 2, which was prepared by the Small Business Committee of the U.S. House of Representatives.

In technical terms, the correlation between real interest rates (e.g., the nominal rate minus the inflation rate [GNP deflator] was 74.5 percent during the 3-year period coverd by the chart and 73.47 percent for the 5 years from 1976 to 1981. Economists say that 74 percent constitutes a "direct and significant correlation" between these two factors.

Higher interest rate movements can affect a business directly and indirectly in several ways. They add to the costs of financing the production, distribution, inventorying and sale of merchandise. They are also a factor in willingness of consumers to purchase the product.

Interest rates also impact general economic conditions with multiple effects on small firms.

A statistical "correlation" does not spell out how two factors relate to each other or what other factors may be involved. But a correlation does indicate some kind of a relationship -- in lesser or greater degree -- and a correlation as high as 74 percent indicates the relationship is close and meaningful.

The plight of industries composed mostly of small firms which are particularly sensitive to interest rates -- such as builders and auto dealerships -- tend to confirm this relationship.

Thus, as long as interest rates remain at record rates, it can be expected that bankruptcies will also continue to set new records.

Effects on Employment

The fifteen million small firms in the U.S. which file tax returns account for 55 percent of existing employment (59 percent if farming is included) and approximately 80 percent of all new jobs. Professor David Birch of M.I.T. found that independent enterprises with 20 or fewer employees accounted for 52 percent of net new private sector jobs between 1967 and 1976. Thus, as bankruptcies increase among small firms, job generation may be inhibited, existing jobs threatened, and increased unemployment may result.

Since each one percent increase in the unemployment rate (approximately equal to one million persons) deprives the U.S. Treasury of $25 to $29 billion in tax revenues foregone and benefits paid, increased bankruptcies -- especially among small businesses -- can translate into larger budgetary and economic problems.

The Human Dimension of Bankruptcies

Several years ago, a doctor at Johns Hopkins University researched the social effects of unemployment ("Estimating the Social Costs of National Economic Policy: Complications for Mental and Physical Health" by Professor Harvey Brenner, Joint Economic Committee Print, October 26, 1976).

This study found that during periods of higher unemployment, use of alcohol, hospitalization, suicides, heart attack and kidney disease also showed statistical increases.

Such an analysis could apply not only to employees, but to small business owners. Entrepreneurs would also be subject to great financial and personal stress in attempting to save businesses in which they have invested a significant amount of their savings and their careers, especially if these efforts were unsuccessful.

According to an attorney who has practiced bankruptcy law for 42 years, Samuel Greenbaum of Washington D.C., many small businesses are under-capitalized to begin with. As a result, such owners are often required to put up personal assets such as their homes as additional security for business loans. If a bankruptcy follows, an owner can also have his family life shattered, exacting a "toll of personal tragedy".

The surge in business failures is therefore of great concern for both economic and social reasons.

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Exhibit 1

BUSINESS FAILURES

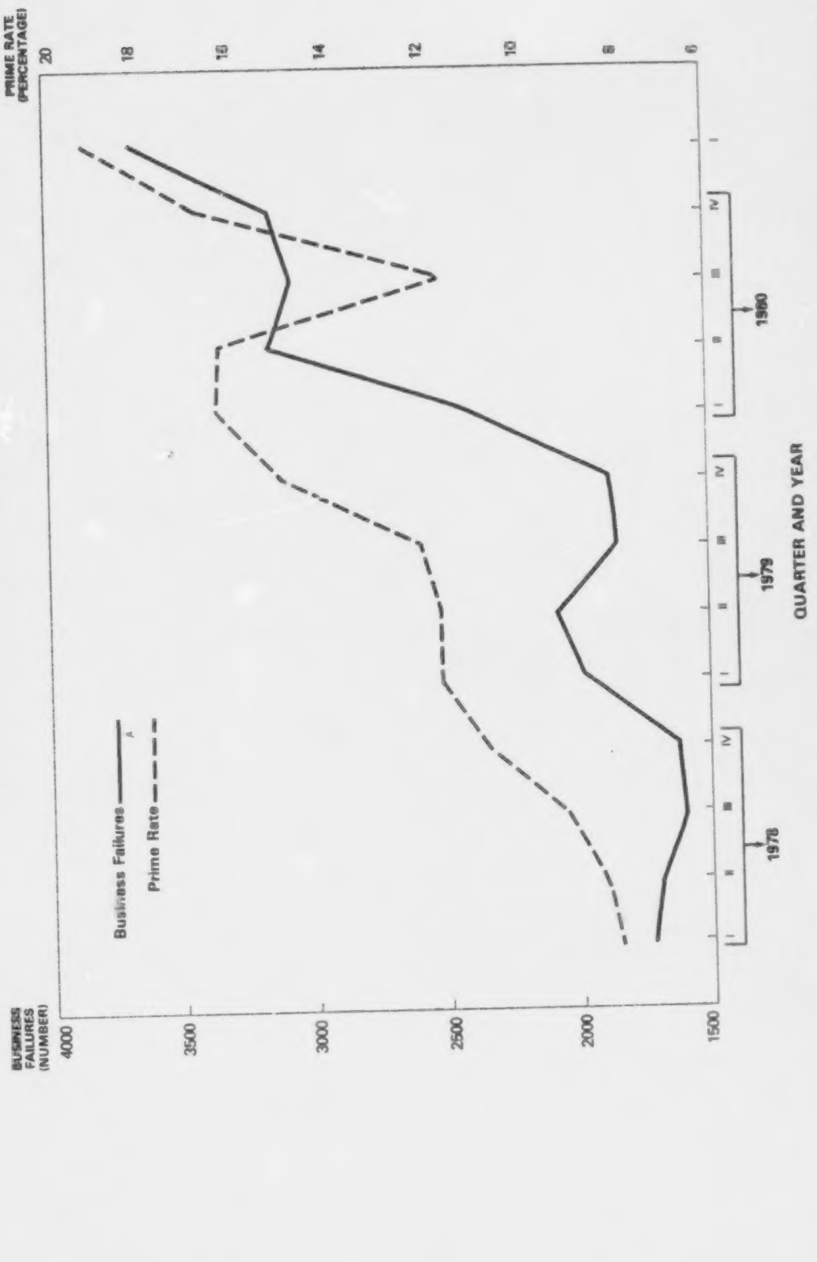
According to U.S. Courts	
1950	8,352
1951	7,387
1952	6,542
1953	6,772
1954	8,888
1955	9,185
1956	9,478
1957	10,144
1958	11,403
1959	11,729
1960	12,284
1961	15,241
1962	15,665
1963	16,303
1964	16,510
1965	16,910
1966	16,430
1967	16,600
1968	16,545
1969	15,430
1970	16,197
1971	19,103
1972	18,132
1973	17,490
1974	20,747
1975	30,130
1976	35,201
1977	32,189
1978	30,528
1979	29,500*
1980	36,443*
1981	47,414*

According to Dun & Bradstreet	
1950	9,162
1951	8,058
1952	7,611
1953	8,862
1954	11,068
1955	10,969
1956	12,686
1957	13,739
1958	14,964
1959	14,053
1960	15,445
1961	17,075
1962	15,782
1963	14,374
1964	13,501
1965	13,514
1966	13,061
1967	12,364
1968	9,363
1969	9,154
1970	10,748
1971	10,326
1972	9,566
1973	9,345
1974	9,915
1975	11,432
1976	9,628
1977	7,919
1978	6,619
1979	7,564
1980	11,742
1981(thur Sept. 3)	11,076

* Exclusive of Joint Petitions

Exhibit 2

BUSINESS FAILURES AND PRIME RATE



SOURCES: FEDERAL RESERVE BULLETIN, DUN & BRADSTREET

Mr. NOWAK. Our next two witnesses will not be in any order of importance, certainly, but they're very patient and I appreciate their staying to the end of this hearing, because they have, I'm sure, very important input not only into this committee but into all the other major committees in Congress. Of course I'm speaking of the NFIB and the Chamber of Commerce of the United States, and if Eamonn McGeady would come forward and John Motley, we'll receive your testimony at this time.

Mr. McGeady is president of Martin G. Imbach, Inc. of Baltimore and he's chairman of the legislative action committee of the chamber's Council of Small Business. He's accompanied by Dr. Ronald Utt, associate chief economist for the chamber, and David Franasiak, director of tax policy, and I welcome Mr. Franasiak, and we look forward to his testimony. Mr. McGeady?

TESTIMONY OF M. EAMONN McGEADY, PRESIDENT, MARTIN G. IMBACH, INC., ACCOMPANIED BY DR. RONALD UTT, ASSOCIATE CHIEF ECONOMIST, CHAMBER OF COMMERCE OF THE UNITED STATES AND DAVID E. FRANASIAK, DIRECTOR, TAX POLICY CENTER

Mr. McGEADY. Mr. Chairman, my name is Eamonn McGeady and I am president of Martin G. Imbach, as you indicated. We are a heavy construction firm that employs about 80 people, to give you some concept of the size that we're dealing with here in the construction industry.

With the committee's permission, I would like to ask that the chamber's printed testimony be accepted for the record and, in the interest of time and particularly of the subcommittee's time, we will not read it verbatim.

Mr. NOWAK. Without objection, it will be submitted for the record.

[Mr. McGeady's prepared statement follows:]

PREPARED STATEMENT OF M. EAMONN McGEADY, PRESIDENT, MARTIN G. IMBACH, INC., BALTIMORE, MD.

Good morning, my name is M. Eamonn McGeady, President of Martin G. Imbach, Inc., Baltimore, Maryland. We are a small business involved in marine and heavy construction. I am a member of the Council of Small Business of the U.S. Chamber of Commerce and serve as Chairman of the Council's Legislative Action Committee. Accompanying me is Dr. Ronald Utt, Associate Chief Economist for the Chamber, Mr. David E. Franasiak, Esq., Director of the Chamber's Tax Policy Center.

The Chamber of Commerce of the United States is the world's largest business federation, comprised of more than 174,000 business firms, 2,700 chambers of commerce in the United States and abroad, and 1,300 trade and professional associations. Small business is heavily represented in our membership. In fact, over 90 percent of our business members have fewer than 100 employees. On behalf of the U.S. Chamber, we welcome the opportunity to discuss the impact of high interest rates on small business capital formation.

There is little need for me to review in much detail the interest rate predicament that now confronts businessowners, consumers and public officials. Over the past several months, interst rates have moved from one record level to another. What is worse, unlike past credit crunches that were widely-spaced and generally of a short duration, this one has persisted, off and on, for a period of several years. Recent interest rate levels have represented a new peak in a three and a half year period of steadily escalating interest rates.

For many businesses, especialy the small ones that are relatively more dependent upon short-term debt, effective defensive measures have long since been exhausted in this three year battle with high and rising interest rates. In many cases, they have been forced to pay several points above the prime rate for needed short term financing. The signs of stress are all too evident. So far in 1981, business failures are 42 percent higher than in 1980, which in turn, were 55 percent higher than the number that occurred in 1979. In 1980, the number of auto dealerships declined by 1,600, as reduced auto sales adversely affected both the dealerships and some of America's largest corporations.

As a representative of the Nation's largest business federation whose vast membership is drawn primarily from the small business community, I am painfully aware of the problems that these interest rates have caused. Letters and phone calls complaining about high interest rates have been streaming into the U.S. Chamber's Washington headquarters. Frequently, these communications are from business that are about to go under unless a significant reduction in interest rates is quickly forthcoming.

Despite the enormous pressures on us to seek and promote some type of public policy remedy that would give the appearance of providing immediate interest rate relief, the Chamber remains steadfast in its support of the four basic components of President Reagan's Program for Economic Recovery. Our continued, enthusiastic support for this program stems from our firm belief that is is the only program that can both guarantee low interest rates and contribute to the solution of the many other problems that have plagued our economy for much of the past decade.

For some, this position of support has become increasingly difficult to maintain in an environment of rising interest rates. That this weakening of will should occur is not surprising: our past failures to adequately deal with our many economic problems can be attributed to an absence of will. The stop-go policies of the past that followed from this weakness are a primary reason why the credibility of policymakers, both in Congress and the Executive branch, is being questioned by financial markets.

Fighting inflation has never been an easy task, as the history of our efforts and the efforts of other nations has amply demonstrated throughout this century. It has required an unwavering commitment to price stability and willingness to accept the adverse side-effects, which are always temporary, that often follow sustained efforts to achieve this objective. That our government remains firmly committed to this objective in the face of immense political pressures should be cause for optimism. It tells us that every effective measure is being taken to reduce inflation, and that the decline in the rate of inflation that we have experienced so far can be expected to continue into the future. And with this reduction in inflation will come decline in interest rates and a resumption of rapid economic growth.

If this is valid, one may very well ask why interest rates have not yet fallen as much as they have. I have no really good answer to this question. Given our general understanding of the fundamental determinants of interest rates, there is no justification for rates to be as high as they are. As I reconsider the Program for Economic Recovery and compare our present experience with similar events in the past, I remain convinced that the current financial market problems are in no way related to any fundamental flaw in the Reagan program. Rather, I believe that today's interest rates stem largely from the actions of a deeply worried financial market that remains skeptical about the determination of public officials to see this program through, and their willingness to continue to make the difficult choices that will be necessary to control government spending and reduce inflation.

If we consider the events of the past three years, we can understand why financial markets remain skeptical about a new government initiative to reduce inflation and restore economic stability.

From the beginning of 1977, interest rates have risen continuously, in lock step with the accelerating rates of inflation that occurred over the same period. In this kind of environment, any investor who committed his funds, for all but the shortest period of time, suffered a capital loss. Indeed, anyone who purchased a long-term corporate bond in early 1977 now holds a debt instrument worth only half what it was on the day of acquistion. Those investors who did make such commitments during this period did so under the optimistic assumption that inflation would be controlled and that interest rates would fall or hold steady. They were sadly mistaken.

In contrast, any investor who held the most pessimistic of assumptions on the outlook did rather well. By taking a defensive position in short-term instruments, these investors preserved their principal and earned high interest rates. And they were never wrong. With this as background, we see that the last three and a half years represented a triumph for pessimism and a sustained defeat for optimism, a defeat measured in the multi-billion dollar loss of value in depreciated bond and loan portfolios. It is not surprising then, that such pessimism should continue to characterize investor attitudes. Despite investor support for the Reagan program, these well established habits of extreme caution will be difficult to break. Financial markets are still not convinced that government is serious about reducing inflation and restoring economic stability.

While this analysis seems to contradict the conventional wisdom that now appears in the financial press, a review of the various reasons used to explain why interest rates are high suggests to me that high interest rates are a problem in search of a cause. Indeed, we have seen a host of ever changing causes being cited as the reason. Since last November, these causes have included "the President's program is inflationary", "economic growth is too strong", "monetary growth is too high", "monetary growth is too loose", "the deficit is too large", "the new budget cuts are too small", and on and on. By and large, each of these alleged causes have been shown to be without foundation. Yet, the search goes on the interest rates remain high.

Perhaps when financial markets run out of spurious causes and finally become convinced that the President and the Congress are serious about controlling inflation, interest rates will break and begin the fall to the lower levels that are consistent with the success we have had against inflation and the absence of any substantive risks in the economic outlook.

As the result of the progress made in reducing the rate of inflation, I believe that interest rates will continue to fall, that they will decline steadily over the next several years and that the President's program is the best approach to the problem. While this is small consolation to the businessowners and consumers who are now severely pressed by high interest rates, there is simply no alternative to the present course. Credit controls have been shown to be a dangerous tool of economic policy, and any significant loosening of the money supply will rekindle inflation and lead to even higher interest rates. Both will damage the small businessman. Worse, such policies would further diminish the credibility of government policy and reinforce the mistrust now so pervasive in financial markets.

In the last several months, we have paid a heavy price to wring out four years of inflationary excesses. To lose our will now would be to squander all that we have gained and all that we are about to gain in the fight against inflation.

As I stated earlier, fighting inflation has never been an easy task. Too often, when the painful side-effects of the fight begin to dominate our perspective, we tend to lose sight of the objective and to forget how damaging inflation has been to our economy. It is all too easy to look at the present situation and conclude, falsely, that the adverse effects of inflation were never as bad as those associated with high interest rates. These interest rates are a legacy of our inflationary excesses, and a failure to get to the root of the problem will guarantee their persistence will into the future.

In many respects, some of the problems now attributed to high interest rates are really problems of inflation. Consider the automobile market which many have cited as an industry bearing the brunt of high interest rates because of the heavy reliance on credit sales. According to a recent Federal Reserve Board analysis, from the end of 1979 to the spring of 1981, escalating interest rates added only an extra $9.00 to the monthly payment on a three year car loan, while the $1,900 increase in the sticker price added about $44.00.

In the housing market, where interest rates are an even more significant determinant of sales, the direct effects of inflation on affordability are just as important. From 1974 to 1981, the average price of existing homes more than doubled rising by 144 percent, while household incomes rose by only 74 percent.

This, of course, is not to say that the interest rate problem is overstated. It is a very serious problem, but the adverse effects of inflation are just as debilitating to our national well-being. Once we make sustained progress against the latter, progress against the former is certain to follow.

While the Chamber remains fully supportive of the President's program, we recommend a few additional steps that will help diminish the pressure on credit markets and allay some of the concerns that are shared by financial market participants.

First, we recommend further reductions in fiscal year 1982 budget outlays. We support the President's most recent cuts and urge Congress to adopt them.

Second, we urge Congress to exert better control over the vast array of loan and loan guarantee programs that have been expanding at a rate in excess of the growth in budget outlays. Like the deficit, these lending programs compete with the private sector for funds and add further upward pressure on interest rates.

Third, while we are fully supportive of the Fed's policy to slow the growth of the money supply, we feel that efforts should now be made to keep monetary growth within the middle of the target range. Given the past excesses in monetary policy, holding monetary growth below or at the low end of the range for any length of time necessitates a sharp adjustment for the economy that my lead to unintended instability and excessive stringency.

These are only minor points, however. The key to success is still the President's program. Without it, our economy would continue to plod along in a path of stagflation with high interest rates and high inflation. We have already made substantial progress in solving the latter problem, and more will follow. If we give up now, or substantially alter the program, this investment will be wasted.

Mr. McGeady. I think, Mr. Chairman, it should be pointed out, particularly at this point in the testimony, that when you're talking small business, you're talking some 13 million, depending on whose numbers you believe, firms, individual proprietorships, partnerships, corporations. In order to put the entire discussion into perspective, if we were to have one-half of those firms hire only one new person, we would have essentially no unemployment. There would remain only about 3½ million structurally unemployed.

Since small businesses account for well over 90 percent of the jobs created in the economy, the question about interest rates is of severe importance, as you have heard already today.

At the outset of my remarks, I'd like to point out that we at the chamber believe that the best method of bringing down interest rates is to continue and to push even harder on the President's economic package, specifically concentrating on the reduction of budget deficits. From my own perception, as I see it, out in the hustings, we in the small business community will make our decisions based upon what we see as being individually best for our firms and our employees. Those perceptions are very important because our decisions will bear fruit 3, 6, 9 months 1 year down the road. In this regard, I think the committee and, indeed, the Congress, should be careful of something that I'm afraid has been ingrained to all of us by Madison Avenue over the years—instant gratification, we expect instant gratification on the reduction of interest rates, but we must be careful that we don't take actions in the short run that lead to very bad results. The recommendations that we propose are found on page 7 of the testimony and those recommendations relate specifically to the further reductions in fiscal year 1982 budget outlays. We urge the Congress to consider those reductions and to adopt them.

Second, we urge the Congress to exert better control over the vast array of loan and loan guarantee programs that have been expanding at a rate in excess of the growth in budget outlays. Like the deficit, these lending programs compete with the private sector for funds and add further upward pressure on interest rates. You heard just before my testimony, Wilbur Doyle, who pointed out that if small business, as part of the private sector, can compete reasonably, we would make out all right. But when we are not able to compete reasonably, we have problems. As an example, we talk about prime, but as you well know, very few small businesses borrow at prime. Most are at 1 point, 1½ points, 2 points above prime.

If you take today's prime, which is 18 percent, today's Federal discount rate, which is at 14 percent, and the average cost of funds to a bank which is probably in the 11 percent range, a little bit of arithmetic shows that small businesses are paying better than a 9-point spread, in most instances. That is an extreme spread.

In our industry, the construction industry, according to Engineering News Record, the average profit margin is 4.2 percent. The construction industry is one of this country's very basic industries. Clearly, when you have, particularly for the small businesses, a 9-point spread, you can immediately see the devastating impact on small business profits.

Third, we are fully supportive of the Fed's policy to slow the growth of the money supply and we feel that the effort should now be made to keep monetary growth within the middle target range. As you probably know the rate indicate that the Fed has gone below its target range, but is now, hopefully, coming back up a little bit toward it.

Given the past excesses in monetary policy, holding monetary growth below or at the low end of the range for any length of time will necessitate a sharp adjustment for the economy that may lead to unintended instability and excessive stringency.

I believe that these points, however, are really subservient to the key point, and that is that the budgetary restrictions and the decrease in the deficit—are the principal, if not the only signals, that need to be sent to the private sector. The financial markets, as is discussed earlier in the testimony, are still not convinced that the Government is serious about reducing inflation and restoring economic stability.

If and only if the Congress sends to the private sector and the financial markets the signals, "We are serious, gentlemen, about reducing inflation and the deficit," then you will see a reduction in interest rates and a resumption of noninflationary economic growth.

I would ask that each member of the committee be provided with the chamber's testimony. I will, of course, make myself available for questions.

Mr. Nowak. Thank you very much.

The points that you've made, I think, have been traditionally what many in Congress have been urged to do by business in general. And yet, we see the stock market and I think you know what the realities are. It has almost come to be meaningless in terms of what the perception is. In other words, the perception is different than the realities but the perception still is going to carry the day, so to speak. I think the program that has been recommended has some merit if we could make some adjustments, and everybody in Congress has, of course, a different idea of where the budget should be cut and where, perhaps, it should be increased.

The President's program has taken, I guess, a compromise between the monetarist view of the world here and what we should be doing at this point in time and the supply side theorists, who, I understand, have some great reservations about raising taxes. I'm sure there is going to be some lobbying done on behalf of some business interests here who are going to have an increase in user fees, user taxes, those kinds of things, and their arguments to us, of course, are going to be, "If you burden us with new taxes, we're going to raise prices. That's going to lead to more inflation." That, of course, was the $3 billion that the President recommended in round terms, although he didn't specify what burden would be or how that the burden would be shared except by talking about the users tax.

I understand Wall Street's reaction and the disappointment after the first budget resolution was passed and, in fact, contained higher cuts than the President recommended to the Congress. At the same time, I think the tax cut was also higher than was recommended, but the supply side theory is, of course, we don't have to worry about deficits, as we had been.

I guess what we're struggling with is trying to decide which theory we can use to get some stability out there. That's a common thread, and I wondered if we do go at this, would it be upsetting to the small business community if we increased the defense cuts instead more of the domestic cuts? Is the perception out there if that were cut, in broad terms, favorable?

Mr. McGEADY. Mr. Chairman, I'm reminded of the old saw about the definition of a recession versus a depression. A recession is when the other guy doesn't have a job and a depression is when you don't have a job. I suspect that across-the-broad spectrum of small businesses, the perception of whether you should cut the guns or cut the butter would be expressed exactly in those terms. Small business, after all, is, in effect, a broad cross section of the Congress' entire constituency. So, I really can't give you a definitive answer except to say that whether we cut defense or domestic, it seems to us that whichever you cut, the removal of inefficiencies and artificial restraints on competition, you would see substantial improvement in Wall Street's outlook and the economic outlook in general, whether you happen to be a Keynesian or a supply sider or a whatever.

For example, the Defense budget could be cut, according to the General Accounting Office's numbers, by close to $1 billion simply by suspending the provisions of Davis-Bacon. But that, of course, is a politically touchy subject. Let's face it, the Congress is going to have to deal with subjects like that which are very basic bread and butter issues.

Another area in which there is ample room to improve employment, and increase revenues to Federal, State, and local governments, would be in either a reduction of the minimum wage or the establishment of a dual-rate structure for the minimum wage. In the city of Baltimore, we now have close to 65-percent unemployment among black teenagers with absolutely no hope of, for example, my company hiring any of those young men and women. I have to pay an unskilled teenager walking in my door a minimum wage that exceeds the value of his contribution to the business.

Under the Davis-Bacon provisions, I have to pay that young man or woman close to $11 an hour if we happen to be working on Federal or State or city projects.

I'm digressing somewhat, but the point is that there are many, many areas of budget cuts that can occur if the Congress will say to its constituency, "By goodness, we are ready. We are going to do this and we are going to have as a national policy the elimination of wasteful and disruptive programs and requirements."

If you ran your office, or if I ran my business, or any of us ran our households on these wasteful procedures, we all know the disaster which would occur. It's the old adage of when your outgo exceeds your income, your upkeep becomes your downfall. That's what we've been doing for too long.

Mr. **Franasiak**. Mr. Chairman, may I add that you raised the point of perception on Wall Street. May I just posit that Wall Street's sense of timing is a matter of a day, at the most, and probably an hour-by-hour at best. These perceptions change in terms of the overall market; the market responds or the market doesn't.

In addition, when one talks about deficits, one must also ask the question of how these deficits are financed, and one of the worst ways for a deficit to be financed is for that deficit to be, in effect, monetized and have the Federal Reserve, in effect, increase the money supply. If that deficit is financed through increased savings, there will not be an inflationary effect.

We believe that this tax cut that was just passed and which is not fully in effect has some provisions in it which are going to really stimulate the overall rate of savings, and which will tend to blunt the effect of this deficit. This is not to say that we're not concerned about deficits, but I think it has to be placed in the proper context.

Mr. **Nowak**. That's a good point. One of the previous witnesses, Mr. Cobb, talked about this subject. I don't know if you were all here in the room. He talked about the deficit and said the deficit is not a problem and that we're going entirely in the wrong direction in considering it. He presented to us a chart which I had been somewhat familiar with prior to this in terms of showing where the deficit, instead of being a larger part of the picture in our economy, is actually defined as a percentage of the gross national product and to the extent where it's lower today than it was in 1953, 1958, 1971, or 1968, the sixties, when we had sustained growth in the economy and a much higher percentage of debt.

It can be shown that GAO had budget figures a few years ago, or 2 years ago when we were wrestling with the same question that if we were to reduce the deficit by either $25 billion or $30 billion—that we would affect the inflation rate by two-tenths to three-tenths of 1 percent. At the time the inflation rate, I think, was 13.2 percent.

That's all on one side. But on the other side you still get the general feeling that the perception is not of that and that the economy moves by psychology or perceptions and the financial impact of reducing the deficit by $14 billion or $13 billion is not going to have the consequence of bringing down the inflation rate 2 or 3 percent.

I don't know if Wall Streeters, with Simon and Greenspan, are sitting up there believing it really is or if they're really more concerned with the perception of what's going to happen and recommending action.

Mr. **McGeady**. But, Mr. Chairman, it seems to me, following that argument for just a moment, that if the man in the street, the man who is looking for some place to put some discretionary funds, whether it be for college tuitions or to buy a house or to buy a boat or to pay off his charge accounts, if he sees that it is going to pay him and he perceives that inflation will be brought under control or substantially reduced, then he is going to go more toward the savings side of the ledger than toward the consumption side. This obviously, will reduce the inflation rate. Moreover, this is the purpose of the tax cut.

Mr. **Nowak**. The delay.

Mr. **McGeady**. With respect to a delay in the tax cuts, something that I've not seen discussed too much with respect to small business people is this: A small business person who has excess funds does one of two things with them. Either they are invested in his or her own business or new capital equipment and expansion, or they are taken out as income. In either case, the economy wins in the sense that if it is taken out as income, discretionary income, then it is taxed under the Internal Revenue individual tax rates. If it is plowed back, it results in some improvement in the overall economy in the form of capital formation, jobs formation, and so forth.

So, my argument would be leave the tax incentives in place and then look toward the reduction of deficit spending.

Mr. **Nowak**. In the defense area.

Mr. **McGeady**. Possibly.

Mr. **Nowak**. Go ahead, Rick.

Mr. **Centner**. I don't know if Mr. McGeady ought to answer this or Dr. Utt should, and Mr. Zayas may want to respond, too. But, what we're talking about here, especially in your third point having to do with the money supply, has a lot to do with the definition of the money supply which, as you recall, was questioned by Mr. Cobb earlier. And I think it has a lot to do with the Newsweek article that you referred to.

Should substitutes for money, substitutes for M1-B be included in the definition of the money supply and, if it should, wouldn't that raise tremendously the rate of growth in it?

Mr. **McGeady**. The professionals will answer it. Let me answer it as a layman first, if I may. I had the fortune or misfortune to have had 5 or 6 years of economic training at Johns Hopkins under Carl Crist and others. Some of it rubbed off and a lot of it didn't, I must admit. It was some years ago.

My own personal judgment is that that argument is best reserved for the Halls of Congress and the halls of academia. About 99.9 percent of the folks out there don't give a damn what you call it or how you tinker with it or whatever. All they know is that 5 years ago, when they went to the supermarket on Friday and they counted the bags and divided the bill into the bags, it came out about $7 a bag. Now you go to the supermarket and it's more like $14 a bag.

Mr. **Centner**. I understand what you're saying; but, in your third point, you talk about the Fed's policy. If the Fed's policy is directed at slowing down or speeding up the growth in the money supply, they'd better darned well know what the term "money supply" means; and, it is, in fact, going to affect the number of bags you get at the grocery store. If those money substitutes are adding to the money supply, and the Fed isn't defining it that way, then in effect we're all being cheated, so I don't think it's a trivial question.

Mr. **McGeady**. No, no, I'm not suggesting it's a trivial question. I'm simply saying that whatever you call it and whatever you include in M1-A or M1-B, or M2, or any of the other definitions, it really doesn't make a whole lot of difference to the average American.

Now, it does make a difference, obviously, as to the Fed policy. If the chairman says money supply and Dr. Utt says money supply they presumably mean the same thing in that exchange. As long as we understand that, my own layman's opinion is that it doesn't make any difference what you put in the pot as long as all know what pot we're talking about.

Mr. CENTNER. Except we'd better have the pot that's really the one that affects inflation.

Mr. UTT. I think to answer your question specifically, is money tight or is money loose, the key measure of the money supply that influences, or is likely to influence, inflation is M1-B, not M2. In that case, money is tight. Money, as measured by M1-B, has grown at minus 1 percent since April. I recognize that M2 is well outside the target bands and, indeed, has been accelerating at a rapid rate. However, I think you have to recognize that the definition of M2 today is substantially different than what it was a couple of years ago because of the advent of certificates and money market funds. Further, this growth in M2 partly relates to the instability in the financial markets and the preference for all investors to stay short. Money that would otherwise be in stocks and bonds, and thus would not be counted in any monetary aggregate, is now sitting in money market funds and in money market certificates, and is therefore counted as part of the monetary aggregates.

This is not transactions money. This is savings. This is investment money. When the market turns, and when perceptions of interest rates and inflation become a little bit more favorable, then this money will come out of M2 and into the more traditional forms of investment. This will lead to a vast shrinkage of M2.

But I think the changes that occur in this measure have very little impact on the inflation outlook.

Mr. NOWAK. Thank you very much. Could you just stay a few minutes and we'll hear NFIB's testimony. John Motley is here for the organization. He's deputy director of the organization for Federal legislation and Edison Zayas is an economist on the research staff for NFIB. Gentlemen, you're both welcome once again to present your testimony.

TESTIMONY OF EDISON ZAYAS, ECONOMIST, NATIONAL FEDERATION OF INDEPENDENT BUSINESS, ACCOMPANIED BY JOHN J. MOTLEY III, DEPUTY DIRECTOR OF FEDERAL LEGISLATION

Mr. MOTLEY. Thank you, Mr. Chairman. I perceive that there's an advantage to going last. Just about everything that we were going to say has been said already, so maybe we can just submit our statement and call it quits at that.

Mr. NOWAK. Without objection.

[Mr. Zayas' prepared statement with attachments follow:]

PREPARED STATEMENT OF EDISON R. ZAYAS, ECONOMIST, NATIONAL FEDERATION OF INDEPENDENT BUSINESS

Mr. Chairman, I am Edison Zayas, Economist on the Research Department Staff of the National Federation of Independent Business (NFIB). Accompanying me today is John J. Motley III, Deputy Director of Federal Legislation. On behalf of

NFIB's membership, which is in excess of 500,000 member firms, I appreciate the opportunity to discuss the impact that this prolonged period of high interest rates has had on the small business community.

The state of small business is dangerously weak. Over the last year, thousands of small firms have gone out of business, and today many more are just barely holding on. For years now, the balance sheets of small firms have been eroded by extensive periods of sluggish real sales, along with high, unexpected inflation rates, huge increases in energy cost, heavy regulatory burdens, and increased income and labor taxes. The result has been a persistent reduction in working capital, forcing more firms to turn to external sources of funds. As the interest rates paid by these reluctant borrowers has risen with anticipated inflation, cash flows have been squeezed even further. To make matters worse, these cost increases have become increasingly difficult to pass on in the face of weak aggregate demand. In short, for many firms, this prolonged period of high interest rates has been the "knockout" blow after having been severely debilitated by the adverse effects of years of unsound government policies.

SMALL BUSINESS PERFORMANCE AT MIDYEAR 1981

Although many factors have contributed to the weakening position of small business, the high level of interest rates has clearly been the major impediment to the beginning of a sustained recovery among small firms in 1981. Despite the economy's robust first quarter performance (8.6 percent real GNP growth at an annual rate), the April NFIB Quarterly Economic Report (QER) indicated that economic activity among small firms improved only modestly in that period. Dollar sales volume and capital expenditures registered only minor gains, while both earnings and employment also recorded only modest improvement from the fourth quarter of 1980. Although prices finally began to moderate, plans to expand business operations in the first quarter of 1981 continued to be thwarted by credit market conditions, as the majority of small firms had to pay close to 18 percent for short-term loans. Moreover, the high cost of carrying inventories associated with those high interest rates resulted in dissatisfaction among small firms with the level of their inventory holdings, despite the fact that they anticipated stronger second quarter sales at that time. As a result, planned inventory additions for the second quarter fell in all industry categories. As expected, planned inventory additions fell the most among firms in the interest rate-sensitive construction and wholesale sectors, where sales have fallen the most.

Optimism Dashed.—Despite the lackluster first quarter performance, however, small business expected overall business conditions to improve in the second quarter. At that time the more upbeat business outlook was based on improved expectations concerning second quarter real sales growth, and credit market conditions, and a more optimistic inflationary outlook. In fact, inflation continued to moderate in the second quarter as anticipated. However, small business' expectations for general improvement in second quarter business conditions, were not realized as the economy slowed abruptly (real GNP fell at a 2.4 percent annual rate) and interest rates escalated further. As a result, the July 1981 NFIB Quarterly Economic Report (the latest to date) showed a decline in both dollar sales volume and net earnings, and for the first time in the history of the NFIB quarterly survey, "Interest Rates—Financing" was ranked more frequently (31 percent) as the single most important problem than any other problem (See Table 1-A). Actual capital expenditures continued to remain flat and to deviate markedly from planned capital outlays (See Chart 1).

Although responding firms did not encounter worsening availability problems in the second quarter, the percentage of firms reporting higher interest rates increased by 13 percentage points from April to July. The average rate of interest paid on short-term loans rose abruptly in the second quarter from 17.6 percent in the first quarter to 19.0 percent. For those borrowing funds tied to the prime rate, the average interest rate paid was 21 percent, up from 19 percent in the first quarter. The overall distribution of rates paid shifted heavily from the 16 percent to 18 percent range to the 19 percent to the 22 percent range (See Table 1-B). In the first quarter of 1981, 27 percent of responding firms reported paying 19 percent to 22 percent on short-term loans. In the second quarter, however, 48 percent reported paying such rates, while the proportion of firms paying 16 percent to 18 percent fell from 46 percent in the first quarter to 34 percent in the second quarter. In addition the few sources of relatively cheap funds all but dried up as the proportion of firms reporting rates below 15 percent dropped from 18 percent in the first quater to 6 percent in the second quarter.

The problems created by these high interest rates have become more intense for small firms who must borrow regularly. Firms operating on small profit margins which must borrow regularly, are forced to reduce other operating costs (e.g. by reducing employment) or they must go out of business. In addition, the combination of a lethargic economy, constantly rising costs (i.e. energy, labor and inventories), and inflation-induced tax increases, has diminished many firms' cash flows to the point where they are engaging in "survival borrowing", that is, borrowing to finance daily operations rather than productivity-enhancing capital expenditures. The high rates charged on loans to these firms have reduced earnings even further.

Firms in rural areas continued to pay significantly lower rates compared to firms in suburban and metropolitan areas, reflecting differences in the cost of funds as well as overhead costs. Forty-nine percent of the firms in rural areas reported paying rates between 16 percent to 18 percent, compared to the 17 percent reporting such rates in metropolitan areas. Nevertheless, even in the rural areas the cost of credit rose rapidly in the second quarter.

Reflecting these rural-urban differences, respondents in the New England-Mid-Atlantic, East North Central, West South Central and Pacific regions reported the highest frequencies of rates ranging from 19 percent to 22 percent. The West North Central region, which had reported the lowest rates in the first quarter, experienced a 26 percentage point increase in the proportion of respondents paying between 19 percent to 22 percent.

These currently high rates of interest rates are making a bad situation unbearable for may small firms. High interest rates are affecting these firms' cash flows directly, and it is difficult to pass these costs on in a weak economy. But high energy costs, taxes, labor costs, and inflation have all taken their toll on small firms, leaving them particularly vulnerable to the cumulative effects of high interest rates.

Due in no small part to credit conditions, real sales growth among small firms, declined moderately in the second quarter, ending three consecutive quarters of reported sales increases. Despite the decline, however, sales remained far above the low reached in July 1980. Nevertheless, the sales slowdown was disappointing since it contributed to the current apprehensiveness among small firms in adding to inventories and expanding business operations.

As a result of the sales slowdown accompanied by higher interest rates, second quarter earnings among small businesses were down from the first quarter. This development augmented the fragile financial status of many small firms since a sustained improvement on the earnings front is critical to relieving the heavy burden being shouldered by these debt-ridden companies. At the same time, the 2.7 percent annual rate of decline in final real sales during the second quarter left firms holding excess inventories. As a result, dissatisfaction with current inventories remained high, forcing a greater proportion of small firms to continue planning inventory decreases than increases. To be sure, uncertainty over future business conditions continues to foster apprehension concerning purchasing commitments, suggesting that little stimulus to the economy, in the form of new orders, can be expected from small business in 1981.

As far as capital expenditures are concerned, the overall picture is one which shows depressed levels of large scale capital investments. Actual capital outlays remained at low levels, with 33 percent making outlays of $20,000, and only 6 percent reporting projects costing over $100,000. Firms are interested and have been interested in expanding their physical plants, but have been prevented from doing so by capital market conditions. The widening gap between actual outlays for plant and equipment and the firms' plans to make such outlays illustrates this problem. Thus, high interest rates and the hope for lower rates in the near future have frustrated small business expansion plans, and prevented the creation of new jobs so badly needed by the economy. Poor economic performance and inflationary expectations continue to raise doubts about the profitability of expansion, which further depresses expansion plans.

Interestingly enough, employment among operating small businesses actually increased by an average of .1 employees per firm in the second quarter, after six consecutive quarterly declines. Although this is a positive development amidst all the gloom, the employment increase was weak and it is likely to remain so over the next quarter. Labor is a major variable cost for small business which can be adjusted to offset rises in the other costs such as materials, energy, taxes and financing. Firms reported that they had to let workers go in order to free up cash to meet these other obligations and keep their firms in business. Skilled labor requirements, which are crucial to the survival of the firms, go unfilled for many small firms. High payroll taxes further discourage the hiring of workers for firms able to add employees. Clearly, before sustained growth in employment in the economy can begin, firm sales must increase, and rising costs which adversely affect the firm's ability to hire labor must stabilize.

Thus, 1981 to date has been especially hard on the small business community. Particularly hard hit have been small firms in industries where sales are dependent on the availability of affordable credit. For small businesses in the automobile, construction, and other durable goods industries, 1981 has been a disaster. Until interest rates fall significantly, firms in these interest rate-sensitive industries will have to fight to stay afloat.

EXPLAINING HIGH INTEREST RATES

Despite the slowdown in the economy and in the rate of inflation over recent months, nominal interest rates have remained at lofty levels. In fact, real interest rates are at the highest levels ever attained in the post-war era. Many have attributed the persistence of these high rates of interest to an overly restrictive monetary policy (i.e., supply factors), to irrational behavior on the part of the financial markets, and to the prospects of continued large federal budget deficits.

As far as the effect of monetary policy on interest rates is concerned, the empirical evidence clearly indicates that high and rising interest rates are in fact associated with periods of excessive monetary expansion, rather than monetary contraction (See Table 2). In observing the period between September 1979 and September 1981, virtually every movement upwards in the three-month Treasury bill rate has been preceded by a sharp increase in the rate of growth of the nation's money supply. Conversely, the majority of downward movements in the three-month Treasury bill rate have been preceded by deceases in money supply growth. During the period encompassing March 1980 through June 1980, M1-B decreased at a 2 percent rate, and the commercial paper rate ended at 8.2 percent in June from 16.8 percent in March. From June 1980 through November 1980, however, M1-B grew at a rate exceeding 15 percent and the commercial paper rate rose to 15.1 percent by November, an increase of almost seven percentage points (See Table 3). Therefore, there can be little validity to the contention that an overly tight monetary policy is responsible for today's high interest rates. If anything can be said about the Federal Reserve Board's policies, it would be that in the past they have allowed the money supply to grow too fast, thereby contributing to high interest rates.

At this juncture, a reasonable question can be posed: given the positive relationship we have observed between money growth and interest rates, why have interest rates not fallen as they have in the past, in response to the significantly reduced money supply growth of recent months? The answer to this question lies in the ignorned demand side of the financial markets. During past periods of monetary contraction, business loan demand declined significantly in response to reduced aggregate demand. This time around, however, short-term business loan demand has remained quite strong despite the slow-down in economic activity, and this is a fundamental reason why interest rates have stayed high for so long (See Table 3).

In addition to this demand factor which has helped to sustain high rates some analysts contend that high interest rates are in part attributable to the hesitant and skeptical disposition of the financial markets where doubts persist concerning the Federal Reserve Board's commitment to permanently reducing inflation. The implication of this argument is that "Wall Street" is somehow behaving irrationally by failing to flood the long-term money markets. To be sure, this collective skepticism does exist, and based on the Federal Reserve's past behavior, it is not unwarranted. The thrust of such skepticism has to do with the degree of downside risk a financial advisor must assess when deciding to commit a client's or an employer's portfolio to a rate of return perceived to be the highest possible, based on the publicized future police directions of the Federal Reserve. If such a decision is based on the often faulty assumption that the Federal Reserve will do what it said it was going to do, the financial advisor's clients or employers stand to lose a great deal of money, and the financial advisor his/her job. One need not go too far back to see that this is precisely what happened to the financial sector. In October of 1979, the Federal Reserve Board announced that it would be pursuing a policy of monetary restraint to reduce inflation, and that money supply growth would be their chief policy indicator. In the following spring of 1980, the Federal Reserve made believers of the financial community when M1-B fell by 1.8 percent from March through June, and interest rates fell below 10 percent. Most members of the financial community believed the Fed would no longer allow money supply growth to become excessive, and as a result, inflation would move steadily downward and that interest rates would not rise again into double digits. This trust in the Fed, however, was shattered as the money supply exploded over the next six months (at one point M1-B grew at a 25 percent annual rate in the summer of 1980), and by year-end 1980, The Treasury bill rate was over 15 percent and commercial paper was earning over 17 percent. In sum, one can easily see why the Fed's announced policies suffer from a lack of credibility, especially in the light of the ever-growing pressure on the Federal Reserve to ease up on the monetary reins. During this "show-me" period, investors are working to avoid being burned as they have been in the past. With confidence so fragile, it is hard to see how a solid market advance can be attained until bonds make a strong recovery based on a convincing and sustained fall in inflation and interest rates.

Finally, many observers have attributed high real interest rates to the perception that the federal government's budget is likely to remain in significant deficit, and that such deficits will place undue pressure on the private credit markets. The concern over the impact of budget deficits on financial market conditions is pervasive. Although there is no apparent causal link between high federal budget deficits and high interest rates (See Table 4), expectations of large future deficits add a strong element of uncertainty concerning the future of availability of capital. In 1980, for instance, the federal deficit amounted to over 60% of total personal savings in this country. As a result, U.S. budget deficits which are small by international standards, evoke alarm in this country because the pool of savings is so small in comparison to countries like Japan and West Germany, where larger deficits present no strain on the availability of capital. Unless the U.S. savings rate increases dramatically and very quickly federal deficits will have to be reduced. Thus, federal budget deficits foster apprehension among institutional and individual investors, which in turn prolongs the recovery of the long-term capital markets. Moreover, the continued existence of budget deficits creates additional uncertainty over the long-term course of monetary policy. As an expansionary fiscal policy continually clashes with a restrictive monetary policy the pressure usually mounts to ease up on the latter.

In brief, it would appear that the prolonged period of high interest rates is in part due to the unusually strong business loan demand experienced this year, and to a perception that the Federal government will back away from its current commitment to reduce inflation. This skepticism has grown particularly acute as pressure mounts on the Federal Reserve Board to effectively finance the burgeoning federal budget deficit by increasing the pace of money creation.

SUGGESTED COURSE OF ACTION

Despite the lack of causality between large federal budget deficits and high interest rates, one must be careful not to interpret that to mean federal budget deficits don't matter. So long as the perception exists that deficits do contribute to high interest rates, it is important to do everything possible to minimize those deficits given the crucial role public expectations play in a market economy such as ours. On more tangible grounds, however, budget deficits must be eliminated because under different leadership and circumstances, the Federal Reserve Board many chose to resume financing those deficits through excessive monetary expansion, which in turn would be inflationary and would lead to higher interest rates. Moreover, federal borrowing needs associated with budget deficits must be eliminated to the extent that federal credit demands strain on already anemic national savings rate. Therefore, NFIB strongly supports all efforts to reduce federal spending activities.

Secondly, although NFIB would like to see the nation's money supply growth at least approach the mid-points of the targeted ranges, we believe that money creation beyond those targets will exacerbate an already volatile situation by fueling inflation and promoting higher interest rates. Monetary policy should remain moderately restrictive. Efforts to reduce interest rates through an overly expansionary monetary policy will be self-defeating.

In addition, we at NFIB feel that given the state of the federal government's finances, Congress should not consider a second tax bill, unless it is revenue neutral. The federal budget must be brought under control before any additional tax cuts are considered. At the same time, Congress must act to limit the federal agency lending activities which add to federal expenditures and contribute to the budget deficit.

In conclusion, it is our belief that all of these steps are necessary to restore the health of our economy. We are encouraged by the recent decreases in short-term interest rates and can only hope that it is the beginning of a sustained downward trend. The small business community will find it hard to survive much longer unless interest rates continue to fall. So long as the Congress and the Administration continue to permanently reduce inflation, interest rates will fall to more tolerable levels.

TABLE 1-A

SINGLE MOST IMPORTANT PROBLEM FOR SMALL BUSINESS

	July 1974	July 1975	July 1976	July 1977	July 1978	July 1979	July 1980	July 1981
Inflation	36%	37%	25%	27%	33%	39%	33%	26%
Interest Rates-Financing	12%	8%	7%	4%	7%	9%	15%	31%
All Other	52%	65%	68%	68%	60%	52%	52%	42%

TABLE 1-B

INTEREST RATES PAID ON SHORT TERM LOANS IN:

Rate Paid	1979	'80:4	'81:1	'81:2
Under 13%	32%	5%	3%	1%
13-15%	28%	22%	15%	5%
16-18%	25%	33%	46%	34%
19-22%		27%	27%	48%
23% or more	7%	4%	1%	5%
Prime +1		5%	4%	4%
Prime +2	6%	3%	3%	2%
Prime +3 or more		1%	1%	1%

CHART 1

PLANNED CAPITAL OUTLAYS

(percent planning capital outlays, next six months)

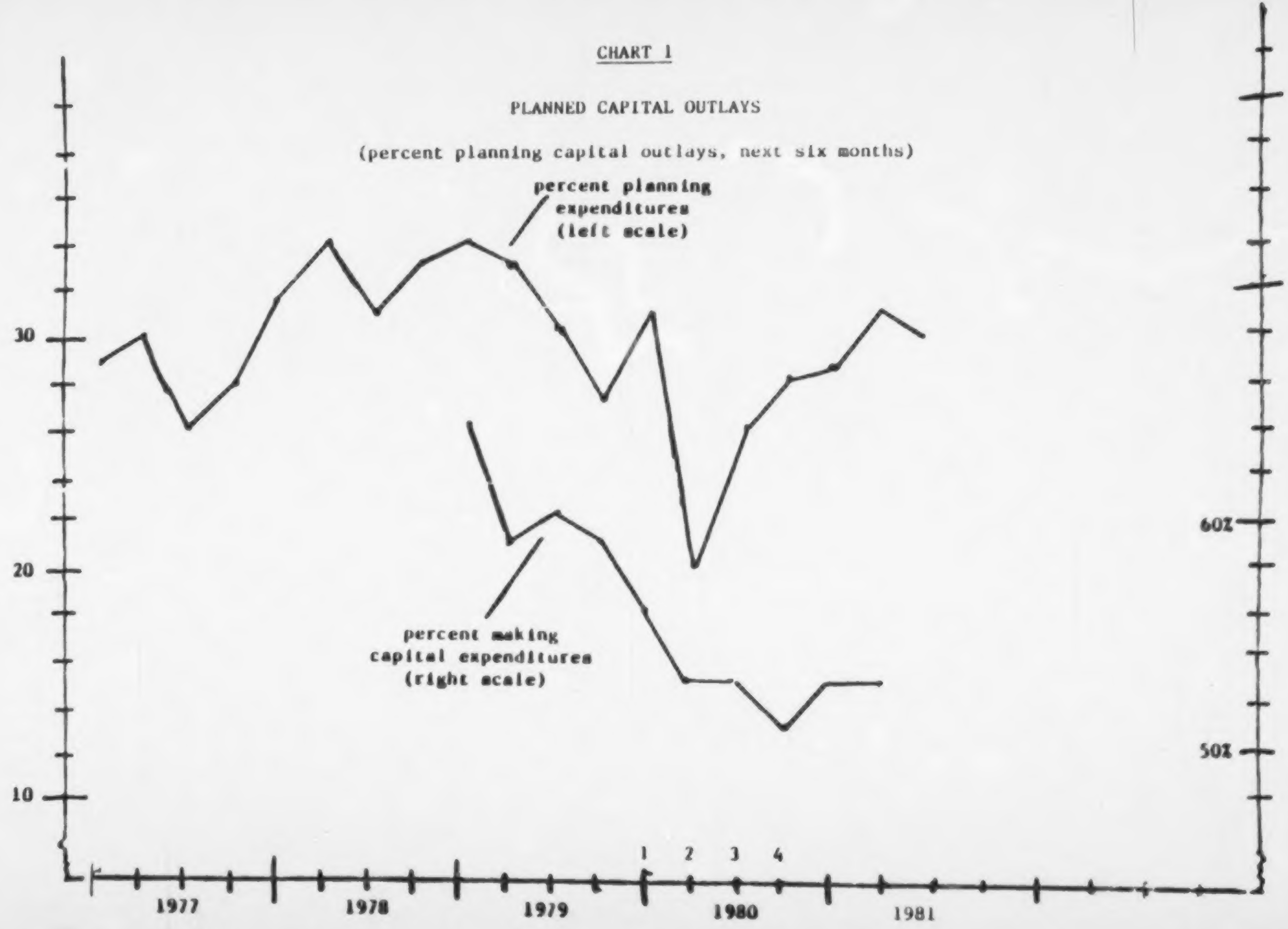


TABLE 2

		M1B	Three Month Treasury Bill Rate
1979 -	Sept.	7.5%	10.3%
	Oct.	1.9	11.7
	Nov.	4.5	11.8
	Dec.	7.8	12.0
1980	Jan.	4.4%	12.0%
	Feb.	13.6	12.9
	Mar.	-0.6	15.2
	Apr.	-15.9	13.2
	May	0.9	8.6
	June	11.6	7.1
	July	14.2	8.1
	Aug.	25.4	9.1
	Sept.	15.4	10.3
	Oct.	13.9	11.6
	Nov.	8.4	13.7
	Dec.	-9.6	15.5
1981**	Jan.	-0.3%	15.0%
	Feb.	-1.4	14.8
	Mar.	8.7	13.4
	Apr.	17.0	13.7
	May	-5.1	16.3
	June	-8.8	14.7
	July	2.6	14.9
	Aug.	6.8	15.5
	Sept.	-0.8	14.3

*Source: Federal Reserve Board Bulletin

**Series adjusted for NOW account shifts

TABLE 3**

Growth Rates of M1B and Business Loans

Period	M1B	Business Loans	4-Month Commercial Paper Rate
3/80-6/80	-1.8%	-9.3%	8.17%
6/80-11/80	15.3	20.3	15.09
11/80-8/81	4.1	12.2	17.03

*Rates as of last month in period.
**Source: Monetary Trends, Federal Reserve Bank of St. Louis.

TABLE 4*

Year	Budget Deficit as a % of Nominal GNP**	Real Rate of Interest
1970	1.2%	1.1%
1971	2.1	-0.7
1972	1.5	-0.1
1973	0.4	1.3
1974	0.8	-0.9
1975	4.5	-3.5
1976	3.1	-0.2
1977	2.4	-0.5
1978	1.4	-0.1
1979	0.6	1.6
1980	2.3	2.4
1981[1]	1.9	6.7

*Source: Economic Report of the President
**Calendar year deficit
[1] Estimate
[2] Yearly average of the three month Treasury Bill rate minus the implicit price deflator.

Mr. **Motley.** Seriously, though, I want to thank you for the opportunity to appear here today to discuss interest rates and their impact upon the small business community and the economic state of that community today.

I also want to thank you and Mr. Marriott and the rest of the members of your subcommittee for a very significant level of activity over this first session of Congress. I think one which surpasses all the other subcommittees on the Small Business Committee and one which I think NFIB and all of the other small business organizations across the country are very grateful for and I hope that you'll be able to keep up a similar pace as we move into the second session.

I really don't think that it's any secret that 1980-81 have been particular trying years for the Nation's small business community. Continued high inflation and record high interest rates have left the community in an extremely weakened state right now and these findings have been emphasized by the recent results of NFIB's quarterly economic report on small business. That report, I think as you probably have heard before, was founded in 1973 and probably is today one of the only measures that is out there showing how the small business community as an aggregate is performing. I'm going to turn it over right now to Mr. Zayas, who is NFIB's economist and who will go over for you some of the recent findings of our latest QER and also explain to you what our position on interest rate policy is.

So, without further ado.

Mr. **Nowak.** Thank you very much. Mr. Zayas?

Mr. **Zayas.** As John Motley said, just about everything that we were going to say has been said, but I think there's been a lack of emphasis concerning one particular aspect, and that's that the big story today is high interest rates. The reason why it's a big story is because the small business community and the business community as a whole has been debilitated and made vulnerable by the effects of the Government policies of the last 10 or 15 years that have resulted in high and volatile rates of inflation, increases in the cost of labor through payroll taxes, increased income taxes, excessive Government regulation, uncertainty concerning the direction of Government policy. All these things have significantly weakened the balance sheets of the small business community, and the prolonged period of high interest rates that we've gone through has effectively been the knockout blow for many of these small firms that have to borrow.

The earnings squeeze that inflation subjects a small firm to forces more firms to seek external sources of financing and it's a self-feeding process, because you have inflation. You have inflationary premiums attached to the level of interest rates and that further aggravates the earning squeeze. So, really, it's not just interest rates. It's all these things put together that have exposed small businesses and made them more vulnerable and now, after a period of 1½ years of high interest rates, the impact is starting to really be felt. As Mr. Motley just mentioned, in the Quarterly Economic Report, our July report interest rates and financing was ranked as the single most important problem by more firms than any other problem, for the first time in the history of the survey. Inflation has always been No. 1.

Mr. NOWAK. Is the result of your survey included in the testimony?

Mr. ZAYAS. Yes.

Mr. NOWAK. What page is that on?

Mr. ZAYAS. It should be in table 1, I believe, although I don't believe the time series was included on the complete single most important problem series, but it does include inflation. Table 1-A at the end of the testimony.

So, principally we're saying that—yes?

Mr. NOWAK. I saw that table, but I wonder if you could break down the other one. Your surveys go from July to July every year.

Mr. ZAYAS. We can provide you more complete times, including month by month.

Mr. NOWAK. Could you give us the breakdown of the others? Where do taxes come out? Do you have a recollection?

Mr. ZAYAS. Taxes typically rank third or fourth, depending on the point in the business cycle that you're at. Usually during good times taxes go up because then you have profits.

Mr. NOWAK. John, do you know the percentage of that?

Mr. MOTLEY. Not off hand, I don't, Mr. Nowak.

Mr. NOWAK. But all other you've got listed here as 42, so that would be some part of that 42?

Mr. ZAYAS. Oh, yes, yes. Included in that.

Mr. NOWAK. The third highest one?

Mr. ZAYAS. It's not always the third highest. It varies. It varies significantly.

Mr. NOWAK. I think we'd be very interested if you could supply that for the record and I would like to carry it right back to July 1974 to show the drastic changes that have occurred from 4 percent to 31 percent. That's dramatic and it shows, I think, what you've testified to, the impact out there.

Mr. ZAYAS. Yes. I think it's important too to recognize the cumulative impact.

Mr. NOWAK. Yes.

Mr. ZAYAS. It's not something that just occurs overnight.

The principal impact has been on the cash flow, the bottom line, and this has resulted in a postponement of capital expenditures. Our firms are telling us that they want to significantly increase capital expenditures. They have heroic plans for capital outlays, but invariably your actual capital outlays differ very markedly from what their plans are, and it's because of the high rates of interest.

Employment has suffered tremendously as well. We have many firms that tell us that if sales improved and if interest rates were to drop, say, 4 to 5 percentage points, that they could do a significantly amount more hiring, but the circumstances are such that they're just prevented from doing so. Those firms that are particularly strapped are forced to lay off people to free up cash so that they can survive. Given that most small businesses are labor intensive, that's the easiest way to free up cash. So, quite clearly, the impact on employment is severe.

I think that as far as——

Mr. Nowak. May I just interrupt you?

Mr. Zayas. Yes.

Mr. Nowak. Do you see the other side of these coins, of course, the unemployment picture. You know it's been stated over and over again, as unemployment increases by 1 percent, the deficit will also increase in terms of approximately $24 billion or $26 billion. I'm just trying to visualize here how fast that employment rate may start to increase if the small business community postpones plans to hire or, if in fact, the labor intensive firm uses the fastest way they can to reduce their inventories of personnel. Is that growth of unemployment going to push us into an even higher deficit position that is already ingrained in the budget process? Are there a growing number of firms reporting back to you that they are reducing their work force?

Mr. Zayas. Actually, the trend has reversed itself as of our last quarterly. In the previous six Quarterly Economic Reports we had net employment declines among our membership. In our July 1981 quarterly we had our first net employment increase, but it was only 0.1 employees per firm, so even though it is a change in the trend, it's still very weak. The critical factor is what's going to happen to sales over the next 6 months and what's going to happen to interest rates. As far as I'm concerned, the real critical variable there is what happens to monetary policy. If the Fed undershoots its targets, as it has done in the past over and over again when the economy starts to falter, then I think you will see, through our Quarterly Economic Report over the next two issues, that the unemployment picture will drop again.

If they maintain their growth targets, the money supply growth within their targets, then I think that you may see continued increases or at least a leveling, staying relatively flat.

The critical aspect is what happens to monetary policy. In the short run monetary policy has a real effect on the economy and we've seen that very clearly.

I think that it's critically important to recognize that interest rates are on the way down. Many people are ignoring that. They have been coming down and all we can do is hope that that's a sign of a sustained downward trend. If it isn't, we're all in trouble, and I think that, what will insure that it is a sustained downward trend is that the Federal Reserve maintain its current posture, whether they increase money and manage to get the money supply growth back within the targets, however you define the money supply. I think that their general thrust cannot be changed.

One of the principal things in addition to this perception that the deficit is creating fears about long-term interest rates, there's a very real fear that exists or that is taking place in, quote, Wall Street, unquote, and that is the downside risks they have to assess in taking a position. They've been burned in the not-too-far-back past, in 1980, the spring of 1980. The Fed made believers of everybody, supposedly, when the money supply growth was actually negative, and people said, "Gee, they really mean it this time." But over that summer and through the fall of 1980 money supply growth exploded and a lot of people in the financial markets really lost their shirts and they haven't forgotten that. The only way you're going to get the financial community to commit itself to the long-term markets is going to be on the back of a sustained downward trend in the rate of inflation and in interest rates, and until then the credibility of the Fed is always going to be in doubt, and that's critical.

We have recommended that in light of these things the Federal Reserve continue the general thrust of its policy, although we would like to see the Fed go to great efforts to avoid undershooting its targets. We want to see continued efforts in reducing the size of the deficit.

On that particular subject I'd like to briefly say that although there may not be an empirical relationship between high rates of interest and relatively high deficits, the fact is that we have a very low savings rate in this country and the size of the deficit in comparison to the size of the national savings in this country is very high. In 1980 it was 60 percent. West Germany and Japan, on the other hand, are capable of running higher deficits because they have significantly higher savings rates. So, when you run high deficits in this country it does evoke fear concerning the future availability of capital, whether it's financed from foreign sources or not, as Dr. Cobb was implying.

Third, we think that Federal lending activities have to be curtailed to help a reduction in Federal expenditures. We would not favor a second tax bill, as the administration previously said it was going to try to implement unless it was revenue neutral, and that's essentially our position.

Mr. Nowak. You mentioned that in your testimony. As you know, when a tax bill gets to the floor there are a lot of changes that take place and I had the opportunity to testify before the Ways and Means Committee. There were a few areas that I wanted to have some impact in and one of them was, of course, a reduction of that spread of the corporate rate up to $250,000 and widening of those brackets to bring down substantially the amount of taxes that would be due for a small corporate owner of a business.

If we had the opportunity to do that, do you think that it still would be a direction we should pursue? I guess what you're saying here is if we can offset that with some budget cuts, whether they be in defense or whether they be in domestic programs, that could still be a way to at least have some corporations form some capital internally.

Mr. Motley. I think that NFIB would always support in concept and in theory further reduction in corporate taxes, probably even the elimination of corporate taxes up to $250,000. In addition to that, as you well know, and I don't have to repeat here, there are some very important things that need to be done in the inventory area, maybe even before we reduce corporate taxes again, because a lot of those firms that are inventory intensive that are out there and are suffering very badly because of high interest rates are not doing business as corporations. They tend to be smaller main street type operations and they're operating as partnerships and proprietorships and so one of the areas I think that the Congress overlooked, although an awful lot of us tried to make them look very hard at it—and you were one of those people who did—was the whole area of inventory reform.

But if you pursue a tax bill before we get the deficit under control and before we begin to move significantly toward balancing the budget as the President and the Congress seem to want to do, I think you're really going to have to look at a neutral bill in terms of changing other sections of the tax codes. Just as a wild example of that, I think there's a story in the Post this morning about the possibility that DISK will go out of business because of GAT and a lot of the business groups and a lot of our large exporters are looking to replace that. It is roughly a billion and a half dollars in revenue loss. You could probably reduce corporate taxes on the bottom end significantly with that $1½ billion.

I think Dave would probably agree with me on that, though I don't necessarily think he'd agree with using the money from the demise of DISK to reduce small business taxes. But those are the types of revenue. You're going to have to do something in one area.

Senator Dole himself has mentioned all-savers certificates. He's mentioned what was done there as far as windfall profits tax and royalties were concerned. There are other areas that I think Congress got into in the bidding war that they would like to go back and revisit. Those are the types of things that could be done to create a revenue bill and to funnel investment in more productive ways rather than in some of the nonproductive things that were done in this past tax bill.

Mr. McGeady. Mr. Chairman, if I may tack onto that, is the reduction, a reduction of rates in the lower end of corporate income, that would certainly be a way to go. I agree with NFIB that has to be accompanied by budget reductions.

Another area that fell between the cracks in the bidding war was the question of investment tax credits on used equipment and here you're talking almost exclusively a small-business item because there are very, very few large corporations that buy used equipment. It's almost exclusively the province of the small businessman, whether he be corporate, proprietor, or otherwise, and I go back again to the little homily of before, that when you reduce rates on corporations, then you use that money in one of two ways: Either, take it out in personal income, which of course is taxed right away, at normally a higher rate than the corporate rates; or leave it to create additional capital, formation of additional capital, either leveraged or nonleveraged.

Mr. Nowak. I guess you could say we have some alternatives and there are some disagreements. I have a couple of questions, especially on the deficit problem. I'd like to submit those to you but unfortunately the bells have gone off again and I'll have to go back, but we'll get to both economists to hear those questions. I really wanted to make them part of this record and see if we can get some broad thinking on that problem, but the cross currents are terrific. If we touched the DISK, you've got some problems on the other side of employment and exporting and so forth. No matter what you do there's going to be a counter effect. If we do have it, I hope we can adjust the tax bill a little better this time than we did the last time, because I think in the feeling of a lot of very conservative Members of the House on both sides of the aisle, if they could do it without a vote they'd like to look at a tax reduction to get a faster balance in the budget.

But on the other hand, if you take away that deduction, you're going to cut back on the amount of money that's going to be available for future investment, and the other question is where does that future investment finally really end up, in the productive sector or in the so-called consumer side of this whole equation.

But, we appreciate your testimony and I wish I could go on further. I've got about 6 minutes.

Mr. MOTLEY. Just one point, Mr. Chairman. The two questions that you've been asking throughout the hearing, one on whether the tax cut should be deferred and, two, deficit spending. NFIB is currently polling its entire membership on both those questions. So, our position is up in the air but we should have the opinion of 70,000 or 80,000 small business people soon.

Mr. NOWAK. We would appreciate the answer and also the answer breaking down the 42 percent.

Thank you very, very much again for spending the time and for your patience with us here as we've gone into the afternoon. Thank you very much.

Mr. MOTLEY. Thank you, Mr. Chairman.

Mr. MCGEADY. Thank you, Mr. Chairman.

Mr. NOWAK. This hearing is adjourned.

[The subcommittee adjourned, to reconvene subject to call of the Chair.]

APPENDIX

APPENDIX A.—PREPARED STATEMENT OF HONORABLE CHRISTOPHER S. BOND, GOVERNOR OF MISSOURI, INCLUDING INFORMATION ON EFFECTS OF REVENUE RULING 81-216

PREPARED STATEMENT OF HON. CHRISTOPHER S. BOND, GOVERNOR OF MISSOURI

I am pleased to appear today on behalf of the National Governors' Association, as the current Chairman of NGA's Committee on Community and Economic Development, to discuss the use of industrial development bonds (IDBs) by state and local governments. As you know, 47 states issue industrial revenue bonds (IRBs) and the principal beneficiaries are small businesses. In fact, the primary utility of IDBs or IRBs is its effectiveness in increasing investment in the smaller firms that provide such a large percentage of this nation's employment and entrepreneurial initiative.

As you may know, Mississippi was the first state to enact legislation, in 1936, authorizing local governments to issue tax-exempt bonds for industrial development projects. The original purpose of those bonds was to promote industrial development and to strengthen the manufacturing employment base of a very depressed, traditional, rural economy. For many years, the use of such bonds usually was aimed at developing and diversifying the economies of relatively poor, rural areas. During the 1960s, they came to be used more frequently to help create jobs or preserve the employment base in major urban centers. As a result of their increased popularity for urban development, IDBs achieved a record dollar volume in 1968. In that year, the Congress acted to curtail their use, and the Revenue Expenditure and Control Act of 1968 has since provided the basic statutory framework for issuance of tax-exempt IRBs. The states adjusted to the restrictions and to their subsequent liberalizations, such as that relating to federal Urban Development Action Grants.

Since 1968, IRBs have been used primarily as a tool to increase capital availability for creditworthy but underfinanced small firms and as a device for attracting business investment or location in otherwise less attractive places. The Fortune 500 and wealthy suburbs have not been the principal beneficiaries of IDBs.

As the dollar volume of IDBs began to increase again, during the late 1970s, due to changes in the federal statute and market factors, the IRB critics came out of the woodwork. During the previous Administration, the Treasury Department delivered testimony critical of IRBs and the Congressional Budget Office raised the spectre of federal revenue loss due to tax exemption.

Now, despite the fact that since 1954 it has formally supported the tax-exempt status of IRBs, the Internal Revenue Service has issued a policy--Revenue Ruling 81-216--that strikes at the innovative use of IRBs to assist credit-short small businesses and struggling small farmers.

Programs in thirty states and Puerto Rico are adversely affected by Ruling 81-216. Twenty-two states stand to lose valuable programs of assistance to small businesses and seventeen will lose their agricultural development programs as a result of this IRS policy.

You should be aware that the effects of Ruling 81-216 are virtually nationwide. This is evidence by the fact that all four regional Governors' associations have passed resolutions opposing the ruling. Copies of those resolutions and other communications from individual Governors are attached as submissions for the record.

This IRS initiative is ironic under an Administration which espouses a return to federalism and has supported liberalization of lease financing, from which IRBs are a financial offshoot. The ruling itself may represent a usurpation of congressional authority by way of bureaucratic rulemaking which exceeds not only the letter, but also the intent, of the law. The procedure employed was certainly deserving of criticism, in that those affected were not forewarned, let alone consulted. In addition, and this is of particular importance to the states, the ruling judges state guarantees of bonds to be equivalent to federal guarantees and denies tax-exemption for those small-issue IRBs that assume the characteristic of a general obligation bond by virtue of a state's unconditional guarantee of principal and interest. This appears to fly in the face of the tenth amendment and the constitutional doctrine of reciprocal immunity.

Congress, rather than the federal courts or the IRS, has acted in the past to limit or expand the tax-exemption of IRBs. In 1914, the Supreme Court decided, in Union Lime Co. v. Chicago-Northwestern Railway Co., that it would not review decisions by state courts concerning what the state government considered to be a promotion of public purpose as defined in its state legislation. The Congress has tended to adhere to a similar principle with regard to decisions by state legislatures. Both have been applied, with few exceptions, to limit federal interference with state authority over the issuance of tax-exempt bonds. However, last year Congress passed the Mortgage Subsidy Bond Tax Act, virtually shutting down state housing finance agency assistance for low- and moderate-income home buyers. Unfortunately, that Act appears to have sent a signal that tax-exempt revenue bonds are fair game. Now the critics of tax-exempt revenue bonds feel that the way is open for them to work their will. Apparently they are in the ascendency at the Treasury Department. I urge you to retake the policy initiative so that the IRB critics do not make the rules of the game for the 1980s. Passage of S. 1635 would be a step in the right direction.

IRBs are an important state and local government financing tool for capital formation and economic development. When virtually all federal economic development programs are slated for termination and many have been eliminated already, IRBs become about the only tool available for financing business development in economically underdeveloped or depressed communities. IRBs are likely to be one of the very few methods by which we can direct scarce credit to small firms suffering from tight money and distressed areas experiencing severe capital shortages.

Tax-exempt industrial development bond financing not only provides small firms an extremely valuable source of needed credit, but also provides state and local governments a "supply-side" tool for promoting economic development that will provide essential employment and income opportunities for their citizens. Without tax-exempt industrial revenue bonds, state and local governments would be left with little meaningful ability to assist small businesses. Most cannot use appropriated funds--general fund monies--or general obligation bond financing as a substitute for industrial revenue bonds. State constitutional and statutory prohibitions against direct financial aid to for-profit firms and general obligation debt purpose restrictions and volume ceilings effectively prevent such substitution.

Both Congress and the Administration have called on the states to take on added responsibilities for community and economic development functions. We are willing, but we need the tools to do the job and the flexibility to use them appropriately.

Economic development needs vary widely among regions, states and localities. If you have seen one distressed community, you have not seen them all. The diversity of development problems underscores the need for IRBs, since absent Revenue Ruling 82-216, they have much of the flexibility necessary for tailoring financial assistance programs to meet state and local realities and priorities.

It is perhaps unfortunate, but nevertheless true, that the tax package enacted this summer is not by any means an adequate substitute for IRB asssistance to small business. In the current monetary policy context, it assists those larger firms that can retain sufficient earnings for self-financing or can publicly issue stock far more than it helps smaller firms that tend to be highly leveraged.

Small businesses, which generally are not in a position to pass on to consumers their increased borrowing costs due to high interest rates, need IRB financing if they are to maintain profitability and avoid bankruptcy. For small start-ups, tax breaks are not of immediate substantial benefit. They do not generate a spontaneous inflow of needed capital to support entrepreneurship. Neither do they make a major difference for most young small firms, since profits tend to be minimum for the first five years and retained earnings tend to be rare. Such is not to say that most, if not all, of the tax reforms aimed at helping small business were not steps in the right direction. It is only to say that other assistance is also needed.

To fill the gap with IRBs, we need access to economies of scale in marketing through pooling of small issues; we need to be able to guarantee issues so that unrated firms can be assisted; we need to be able to deal positively with purchasers' needs for risk diversification in their portfolios. Revenue Ruling 81-216 precludes us from doing so and closes the door on many small businesses.

I appreciate the opportunity to testify on this important issue. I have provided for the record a copy of the NGA policy position in regard to federal legislation governing state and local industrial development bonds. I believe that you will find that it reflects the willingness of the states to accept responsibility for appropriate use of IRBs. We will submit information on the effects of Revenue Ruling 81-216 on specific state programs within the next few days, since time for attorneys' opinions in the various states has been required as part of the impact evaluation.

Extract from NGA Policy Position E-3
Economic Development Challenges of the 1980s: Targeting Resources for Economic Development

FEDERAL LEGISLATION GOVERNING STATE AND LOCAL INDUSTRIAL DEVELOPMENT BONDS SHOULD CONTINUE TO PROVIDE BROAD GUIDELINES WITHIN WHICH STATES CAN MAKE TARGETED USE OF IDBS TO SUPPORT STATE AND LOCAL DEVELOPMENT OBJECTIVES. STATES SHOULD EXERCISE RESPONSIBILITY FOR DEFINING APPROPRIATE PUBLIC PURPOSES FOR IDB USAGE, DETERMINING WHICH JURISDICTIONS OR AGENCIES ARE ELIGIBLE TO ISSUE SUCH BONDS AND ESTABLISHING PROCEDURES FOR THE MONITORING AND REPORTING OF IDB ISSUES WITHIN THE STATE. IN GENERAL, THE PRIMARY PURPOSE OF IDBS SHOULD BE TO FACILITATE INVESTMENTS THAT WILL ENHANCE PRODUCTIVITY AND PROMOTE NEW JOB CREATION WHERE SUCH INVESTMENTS WOULD NOT OTHERWISE OCCUR. STATES SHOULD BE CHARGED WITH THE RESPONSIBILITY FOR ASSURING THAT STATE AND LOCAL USES OF IDBS ARE CONSISTENT WITH THIS PURPOSE.

CONEG
COALITION OF NORTHEASTERN GOVERNORS
400 NORTH CAPITOL STREET, N.W.
SUITE 382
WASHINGTON, D.C. 20001
(202) 624-5440

GOVERNOR DICK THORNBURGH, Chairman
GOVERNOR J. JOSEPH GARRAHY, Vice-Chairman

September 9, 1981

The President
The White House
Washington, D.C. 20500

Dear Mr. President:

On behalf of the Coalition of Northeastern Governors, we wish to register serious concern regarding the effects of Internal Revenue Service Revenue Ruling 81-216 on state industrial development bond (IDB) programs. This ruling, which was issued without prior consultation, eliminates the current tax exemption for multiple lots of small issue revenue bonds of less than $1,000,000 used to provide loans for small and medium size businesses. We believe this revenue ruling is ill-conceived and represents a dramatic step in the wrong direction for IDBs.

The Northeastern states have pioneered the use of so called "umbrella" or pooled bond issues as a way of targeting tax-exempt financing to smaller firms that face particular difficulties obtaining needed capital in the private market. We view the targeted use of this financing technique as a key element of our overall efforts to create new jobs and promote economic revitalization in the Northeast. The effect of this IRS ruling is to severely restrict our ability to provide needed assistance to small firms and farm operators that are hardest hit by current high interest rates.

Congress is currently considering legislative changes to establish more stringent guidelines for state and local IDB programs. In addition, the CONEG Governors recently adopted a policy resolution developed by the CONEG Economic Development Committee, chaired by Governor Hugh L. Carey, supporting reform legislation to ensure the responsible and targeted use of this economic development tool. A copy of this resolution is enclosed for your review. We believe it is a serious mistake for IRS to preempt the legislative process by suddenly reversing longstanding precedents and rulings in this area, and we strongly urge that this ruling be withdrawn.

Thank you for your consideration of this matter.

Sincerely,

Governor Dick Thornburgh
Chairman
Coalition of Northeastern Governors

J Joseph Garrahy
Governor J. Joseph Garrahy
Vice Chairman
Coalition of Northeastern Governors

DT/lw

cc: Secretary Donald T. Regan
  U.S. Department of Treasury
 John E. Chapoton, Assistant Secretary
  U.S. Department of Treasury
 Dan Rostenkowski, Chairman
  U.S. House of Representatives, Ways and Means Committee
 Barber Conable, Ranking Minority Member
  U.S. House of Representatives, Ways and Means Committee
 Robert Dole, Chairman
  U.S. Senate Finance Committee
 Russell Long, Ranking Minority Member
  U.S. Senate Finance Committee
 Northeast Congressional Delegation

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GOVERNOR DICK THORNBURGH, Chairman
GOVERNOR J. JOSEPH GARRAHY, Vice-Chairman

INDUSTRIAL DEVELOPMENT BONDS

WHEREAS, the Coalition of Northeastern Governors regards industrial development bonds as an important economic and community development tool to stimulate capital investment and employment. At a time when federal development assistance is being sharply reduced or eliminated, this financing mechanism must remain available to State and local governments as a development incentive for private investment and;

WHEREAS, we also recognize that legitimate concerns have been raised regarding abuse of small issue industrial development bonds, particularly those issued for commercial purposes.

THEREFORE, BE IT RESOLVED that the CONEG Governors recommend the following changes in federal legislation in response to that criticism:

- Target commercial IDBs to distressed areas by providing broad federal guidelines within which States have the flexibility to determine the targeted areas based on State and local economic objectives.
- Exempt from these restrictions special economic activities which are of particular importance to a specific State's economy and which encompass less than 5 percent of the States's economic base.
- Exempt all production activities from research processing to warehouse-distribution from targeting limitations.
- Establish federal monitoring and annual reporting requirements by States for all small issue IDBs issued in each State.

CONEG CONEG CONEG
COALITION OF NORTHEASTERN GOVERNORS

GOVERNOR DICK THORNBURGH, Chairman
GOVERNOR J. JOSEPH GARRAHY, Vice-Chairman

FOR IMMEDIATE RELEASE
Monday, September 14, 1981

CONEG POLICY RESEARCH CENTER
CONTACT: Connie Saulter
(202) 624-5440

GOVERNORS SAY NO TO IRS RULING ON INDUSTRIAL REVENUE BONDS

WASHINGTON, D.C., September 11 -- Pennsylvania Governor Dick Thornburgh, Chairman of the eight-state Coalition of Northeastern Governors (CONEG) and Rhode Island Governor, J. Joseph Garrahy, Vice Chairman of CONEG, have called for White House withdrawal of a recent Internal Revenue Service ruling that would eliminate the current tax exemption for state industrial development bond pools used to provide loans to small and medium size businesses. The IRS ruling, issued on August 24, would eliminate the ability of states to package a series of small business loans into a single tax-exempt "umbrella" or pooled bond issue.

In a September 9 letter to President Regan, Governors Thornburgh and Garrahy said that the effect of the new IRS ruling will "severely restrict our ability to provide needed assistance to small firms and farm operators that are hardest hit by current high interest rates."

Governor Garrahy noted that the Northeastern states "have pioneered the use of pooled bond issues as a way of targeting tax-exempt financing to small businesses that are shut out of the private capital market." Garrahy cited recent studies which show that small businesses create more than 80 percent of all new jobs in the economy each year, a fact which has led many states to focus on the small business sector in their economic development efforts.

Governor Thornburgh called state industrial development bond (IDB) programs "a key element of our overall efforts to create new jobs and promote economic revitalization in the Northeast." "We believe this ruling is ill-conceived and represents a dramatic step in the wrong direction", Thornburgh said.

Several Northeastern states have used "umbrella" or "pooled" IDB's to finance loans to small and medium size businesses. Rhode Island this year has also initiated a similar program that has already assisted a number of small Rhode Island manufacturers.

Connecticut has issued umbrella bonds totalling $155 million over the last ten years. The Connecticut program has provided assistance to more than 500 small firms, and is estimated to support the creation of more than 9,000 new jobs annually in that state.

New York's umbrella bond program has provided loans to more than 1,200 companies, with total employment of over 90,000 workers.

(over)

WASHINGTON, D.C. 20001 (202) 624-5440

The Pennsylvania Industrial Development Authority (PIDA) has issued IDB's totalling more than $92 million since 1975, the proceeds of which have financed more than 400 loans to firms employing roughly 33,000 workers. Several other Northeastern states have developed plans for issuing pooled IDB's, but have been stopped by the new IRS ruling.

The Governors expressed concern to the President that this ruling hinders possible action by Congress to enact reform legislation governing the issuance of small issue industrial development bonds. In light of this legislation, the CONEG Governors recently adopted a policy resolution developed by the CONEG Economic Development Committee, chaired by Governor Hugh L. Carey, supporting reform legation to "ensure the responsible and targeted use of this economic development tool."

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WESTERN GOVERNORS' CONFERENCE
THE COUNCIL OF STATE GOVERNMENTS
165 POST STREET, 5th FLOOR SAN FRANCISCO, CALIFORNIA 94108 (415) 986-3760

Proposed Resolution E:

URGING THE WITHDRAWAL OF IRS REVENUE RULING 81-216

(Introduced by Governor Victor Atiyeh, Oregon)

WHEREAS, the Internal Revenue Service on August 24, 1981, issued Revenue Ruling 81-216 which holds that multiple lots of industrial development bonds of $1 million each will not qualify for the tax exemption under the Internal Revenue Code Section 103(b)(6)(A) if:

(1) the obligations will be sold at substantially the same time,

(2) the obligations will be sold under a common plan of marketing,

(3) the obligations will be sold at substantially the same rate of interest, and

(4) a common or pooled security will be either used or available to pay debt service on the obligations; and

WHEREAS, the lack of capital available to small farms, ranches and small businesses and the present high rates of interest have placed many farms, ranches and businesses in severe economic difficulty resulting in extraordinarily high rates of bankruptcy; and

WHEREAS, many states in the Western Governors Conference have adopted or are considering adopting programs to assist small farmers, ranchers and small businessmen by making available to them the proceeds of $1 million industrial development bonds or agricultural development bonds which have been issued in multiple lots by a state authority; and

WHEREAS, many states have developed these statewide tax-exempt bond programs to help small farms, ranches and small businesses in reliance upon earlier Treasury Department rulings which are reversed by Ruling 81-216;

NOW, THEREFORE, BE IT RESOLVED by the Western Governors' Conference that, as governors of states which have made concerted efforts to help small businesses and small farms and ranches, we urge the President of the United States to withdraw Revenue Ruling 81-216 immediately to avoid any further damage to those state governments which have relied in good faith upon the earlier revenue rulings and to allow the states to utilize these vital programs which often provide the only affordable or available source of credit to struggling farmers, ranchers and businessmen.

[illegible]
GOVERNORS'
CONFERENCE

Beth

September 1, 1981

JAMES R. THOMPSON
Illinois
Chairman

JOHN CARLIN
Kansas
Vice Chairman

CHRISTOPHER S. BOND
Missouri
Past Chairman, [illegible]

JOHN Y. BROWN, JR.
Kentucky

LEE S. DREYFUS
Wisconsin

WILLIAM J. JANKLOW
South Dakota

WILLIAM G. MILLIKEN
Michigan
Past Chairman, [illegible]

ALLEN I. OLSON
North Dakota

ROBERT D. ORR
Indiana

ALBERT H. QUIE
Minnesota

ROBERT D. RAY
Iowa
Past Chairman, [illegible]

JAMES A. RHODES
Ohio
Past Chairman, [illegible]

CHARLES THONE
Nebraska

The President
The White House
Washington, D.C. 20500

Dear Mr. President:

The Midwestern Governors have asked me to convey to you our deep concerns about the implications of Internal Revenue Service Revenue Ruling 81-216. This ruling prohibits issuanc of multiple lots of $1,000,000 revenue bonds and eliminates tax exempt financing to assist small farmers. The ruling will have the effect of depriving small farmers and small businesses of much needed sources of capital for farmland, equipment and plant facilities.

As Governors of states which have made a concerted effo to help small businesses and small farms, we believe that thi ruling should be withdrawn. State and local governments hav been relying in good faith upon earlier rulings which this announcement reverses, as have many small farmers and small businessmen who are dependent upon the sources of credit which this ruling would eliminate. Hundreds of millions of dollars are involved nationwide in the various loan programs which will be jeopardized by this ruling.

Specifically, the Revenue Ruling would eliminate two for of financing which state governments have developed and tailo to assist small farmers and small businessmen particularly during the past two to three years when credit has been unaffordable or unavailable.

In the first instance, it would eliminate the use of agricultural development bonds, a form of tax-exempt financin used by the states to assist small farmers in the acquisition of farm equipment or farmland. With the sharply diminished role of the FmHA in providing direct or guaranteed loan assistance to American farmers, agricultural development bond have become an important, and in some areas an exclusive, source of credit to allow small farmers to continue their operations.

[illegible]

Thousands of small businesses also will be deprived of credit because the IRS ruling bars the use of a mechanism developed by the states in which state development agencies put together a package of tax-exempt financing and then make individual loans available to new or expanding small companies. This assistance is aimed at small concerns whose credit would be insufficient to give an individual bond issue a rating which would make it attractive to potential investors. However, when the bond for one small company is grouped together with bonds for a number of other companies, insured credit often is available for the entire transaction, making low-cost financing available to companies who would otherwise be forced to retrench to go out of business.

Revenue Ruling 81-216 will have extremely severe consequences for the most vulnerable and some of the most important elements of our country's economy - small businesses and small farms - and we strongly urge its withdrawal.

Thank you for your consideration.

Sincerely,

James R. Thompson
Chairman

JRT:sj

RESOLUTION PROPOSED BY
GOVERNOR CHRISTOPHER S. BOND, MISSOURI

INDUSTRIAL DEVELOPMENT BONDS

Whereas, The United States Treasury Department has announced its intention to issue a regulation denying tax exempt status to multiple lots of industrial development bonds having an aggregate face value of over $1 million if the bonds are: sold at approximately the same time; sold under a common marketing plan; sold at substantially the same rate of interest; and backed by a common or pooled security which is available to pay debt service. The regulation, which will permit 30 days comment and hearings after 45 days, would be effective retroactively August 24, 1981-the date of the earlier IRS ruling 81-216, which has been withdrawn; and

Whereas, industrial development bonds constitute one of the few economic and community development tools left to the states during this period when federal development assistance programs have been sharply curtailed or eliminated; and

Whereas the lack of capital available to small farms, ranches and businesses and the present high rates of interest have placed many farms, ranches and businesses in severe economic difficulty resulting in high rates of bankruptcy; and

Whereas, the decisions of many employers on whether to make job creating investments in new or expanded plants and facilities are frequently based on the availability of tax-exempt industrial revenue bond financing, the elimination of such a financing tool will mean that many new jobs simply will not be created; and

Whereas, many states in the Southern Governors' Association have adopted or are considering adopting programs to assist small farmers, ranchers and businesses by making available to them the proceeds of $1 million industrial development bonds or agricultural development bonds which have been issued in multiple lots by a state authority; and

Whereas, the proposed Treasury regulation is untimely because it is being issued at a time when the Treasury Department is conducting a comprehensive review of tax exempt bonds and Congress is considering legislation regarding industrial development bonds; and

Whereas, many states have developed these statewide tax exempt bond programs to help small farms, ranches and businesses in reliance upon earlier Treasury Department rulings which are reversed by the proposed regulation;

NOW, THEREFORE, BE IT RESOLVED, that the Southern Governors' Association urges the Treasury Department to withdraw its proposed regulation so that Congress has the opportunity to address the issue of industrial development bonds in an orderly and comprehensive fashion

BE IT FURTHER RESOLVED, that the Southern Governors' Association Congress to enact legislation which will permit the states to continue their tax exempt bond programs to create new industrial jobs and to help small farms, ranches, and businesses in a manner which protects the fiscal integrity of the federal Treasury.

COMMONWEALTH of VIRGINIA
Office of the Governor
Richmond 23219

John N. Dalton
Governor

September 9, 1981

The Honorable Ronald Reagan
The President
The White House
1600 Pennsylvania Avenue
Washington, D. C. 20500

Dear Mr. President:

It has just come to my attention that the Internal Revenue Service on August 24 issued Revenue Ruling 81-216 which will result in disastrous consequences for small farmers and small businesses in Virginia by depriving them of much needed sources of private capital for farmland, equipment, and plant facilities.

This action by IRS does not appear to be in the public interest and is counter to your base philosophy of decreasing the burden of federal regulations on the general public.

In February of 1981, our General Assembly passed legislation creating the Virginia Agricultural Development Authority as an expression of the belief that it is in the public interest to assist the State's industry of agriculture. This industry has experienced unfavorable weather conditions in three of the last five years. At the same time, production costs have increased astronomically without a corresponding increase in commodity prices and even our most efficient and productive farmers are finding it increasingly more difficult to break even financially.

With the sharply diminished role of the FmHA in providing direct or guaranteed loan assistance to farmers, agricultural development bonds have become a viable source of badly needed credit for Virginia's largest single industry which is basic to our economy. The floating interest rate on loans made by the Farm Credit Service -- our principal agriculture lender -- has increased to record high levels.

Agriculture is the basis of the American economy and has been more than pulling its share of the load in our international balance of payments; however, we are not at all sure how long this can continue while agriculture continues in this devastating cost-price squeeze while barely eking out an existence.

We believe the American people, as did our General Assembly in 1981, strongly support the idea of private capital being used to finance agriculture and certain small businesses through the sale of tax exempt bonds. We have been optimistic that this new source of capital would be the help that many of our farmers so badly need and deserve.

We strongly urge you to direct the withdrawal of this ruling which we believe will have extremely severe consequences for a vulnerable but very important segment of this nation's economy -- our small farms and businesses.

With all good wishes, I am

Very truly yours,

John N. Dalton

JND/jhw

cc: The Honorable Donald Regan
The Honorable John Block
The Honorable Roscoe L. Egger, Jr.
Virginia Congressional Delegation
Mr. Rich Williamson

STATE OF MARYLAND
EXECUTIVE DEPARTMENT
ANNAPOLIS, MARYLAND 21404

HARRY HUGHES
GOVERNOR

September 18, 1981

SAME LETTER SENT TO: THE HONORABLE PAUL S. SARBANES

The Honorable Charles McC. Mathias, Jr.
United States Senate
358 Russell Senate Office Building
Washington, D.C. 20510

Dear Senator Mathias:

You have recently received a letter signed jointly by your colleagues, Senators Weicker, Durenberger, and Stevens notifying you that they would soon introduce legislation which would delay the implementation of a recent Internal Revenue Service (IRS) Ruling (IR-81-216 dated August 24, 1981). I strongly urge you to support this legislation.

The effect of the IRS ruling is to prevent states from bundling and simultaneously issuing "small-issue" development bonds (IDB) for small businesses and family farms. At this time, Maryland does not have a development bond program for farmers, but the 1981 Maryland General Assembly passed my administration's legislation which created an "umbrella bond" program in the State targeted to small businesses.

It is no secret that interest rates are at record high levels. Access to the tax-exempt bond market can reduce interest cost to borrowers. The "umbrella" bond concept reduces the cost of issuance for the borrowers by spreading those costs among those under the "umbrella."

I am concerned that the problems of capital availability for small businesses will only be exacerbated by this systematic attack on small business. As you know, the Small Business Administration, the Economic Development Administration, and the Farmers Home Administration now have reduced capabilities.

It should also be noted that the Oversight Subcommittee of the House Ways and Means Committee has been reviewing IDB financing and has introduced HR 4420 as a result of that review. I do not support that legislation. However, it seems that the Internal Revenue Service has preempted congressional review with regard to at least the "small-issue" IDBs.

I support congressional review of this matter, and I therefore support the Weicker, Durenberger, and Stevens legislation which would delay implementation of the IRS ruling to give the Congress adequate opportunity to decide the issue.

I would appreciate your assistance in this regard.

Sincerely,

Harry

Governor

EXECUTIVE OFFICE
STATE OF MISSOURI
P.O. BOX 720
JEFFERSON CITY
65102

CHRISTOPHER S. BOND
GOVERNOR

August 27, 1981

The President
The White House
Washington, D.C. 20500

Dear Mr. President:

The Internal Revenue Service has issued a revenue ruling which will result in adverse consequences for the nation's bond market and which will deprive small farmers and small businessmen throughout the country of much needed sources of capital for farm land, equipment and plant facilities. Mr. President, we believe that this action by the Service is in conflict with the public interest; that it is the antithesis of the even handed and consistent policies which you are trying to urge upon all federal agencies in their treatment of American citizens and American businesses, and that it represents a gross abuse of the tremendous power that is vested in the federal agency responsible for fairly administrating our nation's tax laws.

As governors of states which have made a concerted effort to help small business and small farms, we believe that it is critical that this ruling be withdrawn immediately to avoid any further damage to the already weakened bond markets, to the state and local governments which have been relying upon earlier rulings that this announcement reverses, and to the many small farmers and small businessmen who are dependent upon the sources of credit which this ruling would eliminate.

Specifically, Mr. President, the revenue ruling would eliminate two forms of financing which state governments have developed in recent years and tailored to assist small farmers and small businessmen particularly during the past two to three years when credit has been unaffordable or unavailable. In the first instance, it would eliminate the use of agricultural development bonds, a form of tax-exempt financing by the states to assist small farmers in the acquisition of farm equipment or farm land. A recent Business Week article indicated that on newer farms--farms operated by younger farmers beginning a new enterprise--interest costs have doubled in the past two years to account for as much as 30 percent of their total expenses, wiping out most or all of their profits. A Minnesota banker estimates that up to 12 percent of farmers are at their practical debt limit now and another 10 percent are "hurting." At the end of April, one-third of the FmHA's $20 billion in outstanding loans were in arrears, and the Under Secretary of Agriculture says that "people are going to have to restructure a lot of debt."

With the sharply diminished role of the Farmers Home Administration in providing direct or guaranteed loan assistance to American farmers, agricultural development bonds suddenly have become a viable, and in some areas an exclusive, source of credit to allow small farmers to continue their operations and avoid bankruptcy or having to sell their entire operations. According to an Illinois University professor of agricultural finance, "Many bankers and the farm credit system have been willing to lend to marginal farmers because FmHA stood by to bail them out. Now those lenders will be much less willing to make loans."

Thousands of small businesses also will be deprived of credit because the IRS ruling bars the use of a mechanism developed by the states in which state development agencies put together a package of tax-exempt financing and then make individual loans available to new or expanding small companies. This assistance particularly is aimed at small concerns whose credit would be insufficient to give an individual bond issue a rating which would make it attractive to potential investors. However, when the bond for one small company is grouped together with bonds for a number of other companies, insured credit often is available for the entire transaction making low-cost financing available to companies who would otherwise be forced to retrench or go out of business.

Mr. President, this ruling will have severe consequences for the most vulnerable and some of the most important elements of our country's economy--the small businessman and the small farmer--and we strongly urge you to direct its withdrawal. The Treasury Department and the Congress are in the process of examining the use of industrial development bond financing. If the problems supposedly addressed in the ruling do in fact merit restrictive action, the Congress and the Administration can propose action through legislation. We urge you not to allow the Treasury to impose by regulation, an ill conceived, unduly broad, and potentially disastrous restriction on the states and on American businessmen and farmers.

Sincerely,

CHRISTOPHER S. BOND
Chairman, Committee on Economic
and Community Development
National Governor's Association

CSB:sp

bcc: Governor Richard Snelling
Governor James Rhodes
Governor William Winter
Governor Pierre S. du Pont
Governor John Y. Brown, Jr.
Governor Frank White
Governor Brendan Bryne
Governor James R. Thompson
Governor Paul Calvo
Governor Carlos Romero-Barcelo
Jim Davidson
✓Tom Bash
Don Sipple
Dick King
Chip Casteel
J. H. Frappier
David Broeker

M I F A

Robert E. Patterson
Executive Director

IRS/81-216

JCM for
[illegible]

SEP 2 1 1981

September 21, 1981

Steven Farber
Executive Director
National Governors Association
400 North Capital Street, N.W.
Washington, D.C. 20001

RE: Rev. Ruling 81-216

Dear Steve:

I think you should have a copy of the enclosed letter from Governor King to the President regarding a somewhat technical but extremely significant revenue ruling which I know your association has been very concerned about. I have been working with Dave Arnold on this, and I think everyone agrees that regardless of their personal views about industrial revenue bonds, this ruling is no way to deal with the issue.

I would just like to add to our Governor's words that having the ruling rescinded is of the utmost importance to our economic development program. This ruling will have a far greater effect at eliminating reasonably priced expansion capital for smaller companies than would any of the legislative proposals regarding IDBs, including Congressman Rangel's bill. I and the Smaller Business Association of New England have met with Assistant Secretary Chapeton to point out to him the practical effect of the ruling on small business, to no avail.

Please let me know whatever Governor King could do to assist the National Governors Association in its efforts to rescind this very unfortunate ruling.

Best regards,

Robert E. Patterson
Executive Director

REP/pac
Enclosure

Massachusetts Industrial Finance Agency
125 Pearl Street
Boston, Massachusetts 02110
Telephone: 617-451-2477

THE COMMONWEALTH OF MASSACHUSETTS
EXECUTIVE DEPARTMENT
STATE HOUSE • BOSTON 02133

EDWARD J. KING
GOVERNOR

September 16, 1981

President Ronald W. Reagan
White House
Washington, D.C.

Dear Mr. President:

I would like to express to you my extreme disappointment with Revenue Ruling 81-216 announced by the Internal Revenue Service on August 24th. This ruling will have a devastating effect upon our efforts here in Massachusetts to revive our economy by providing affordable credit to growing small businesses through our industrial revenue bond program.

In the face of rising interest rates and shrinking credit availability for small businesses, these bonds have been an essential source of affordable financing to enable new and growing businesses to invest in productive assets in Massachusetts. This investment has been the source of our recent economic resurgence and of a dramatically lower unemployment rate. Rev. Ruling 81-216 will stop dead the expansion of these companies at a time when smaller companies in particular are suffering from the crushing burden of today's interest rates.

This ruling will effectively close off reasonably priced credit for small businesses while leaving the tax-exempt market available for their larger competitors. These unfair competitive effects are indefensible. The ruling will freeze smaller companies out of the national credit markets during a very difficult financial period.

Rev. Ruling 81-216 was announced without notice,and without the opportunity for public comment which a regulation would have provided. It represents a dramatic reversal of prior IRS policy. In fact, it expressly revokes three prior rulings upon which my state has relied while preparing an innovative program to give smaller companies access to the national credit markets. Our program had been announced to the state's banking community. Many of our banks and companies were basing important financial plans on this new program, which was clearly legal under these long-standing rulings now suddenly reversed by the IRS.

Unless Rev. Ruling 81-216 is revoked, it will be impossible for smaller companies to obtain capital from the national credit markets pursuant to the federal law governing industrial revenue bonds. With this ruling the IRS has arbitrarily overruled Congress' explicit favoring of smaller projects and companies for industrial revenue bond financing.

It is a fact that smaller, unrated companies cannot sell bonds in the public markets unless they purchase additional collateral (insurance or bank letters of credit). It is bad enough that these companies must pay higher rates to purchase the collateral they need to buy access to the national debt markets. It is unacceptable, however, that the IRS with Rev. Ruling 81-216 should bar them from these markets on the sole technicality that the additional collateral has been purchased.

At a time when federalism is being given a new lease on life and our nation's policies are focusing on economic revitalization, it is puzzling to see the IRS abruptly halt the efforts of many states to provide reasonably priced capital for smaller companies and farmers adding productive assets and creating new jobs.

As the Governor of a long-distressed state which recently has made business growth the cornerstone of its program, I urge you to reverse this ill-conceived ruling which changes the rules in the middle of the game with no prior notice to anyone and will have disastrous consequences to smaller businesses.

Thank you for your consideration.

Sincerely,

Edward J. King

Edward J. King
Governor

EJK:pjp

kdfa
Kentucky Development Finance Authority

MEMORANDUM

TO: Jim Martin and Bill Bivens
National Governors Association

FROM: Roger L. Peterman
Executive Director

SUBJECT: Revenue Ruling 81-216

DATE: September 30, 1981

During times of high interest rates the first to suffer are the small businessman and the small family farmer. The severe problems are due to limited sources of revenue and to the high percentage of overall costs that interest rates represent. From an economic development viewpoint this problem is quite serious, since small business generates the greatest number of new jobs. High interest rates not only prevent these individuals from expanding into new production areas or modernizing, but in a very real sense pose the threat of insolvency. Unfortunately, the Internal Revenue Service has compounded the problem through Revenue Ruling 81-216.

The Commonwealth of Kentucky has attempted to establish methods of making low interest rate money available to the small businessman and farmer through tax-exempt financing. The only way to make small, tax-exempt, loans is by combining a number of loans into a single industrial development bond issue. Loans can only be combined into single issues by using one common underlying credit for all the loans. Kentucky has explored the possibility of using federal guarantee programs, state guarantee programs, and private sector guarantees to provide the underlying credit. In one instance a program was promoted to the financial community and was very well received, only to be eliminated by Revenue Ruling 81-216.

The best interests of Kentucky and the Nation are served by the small businessman and farmer. The counter-cyclical nature of tax-exempt financing is an efficient way of providing assistance during these difficult times. It is unfortunate that the Internal Revenue Service has adopted a policy that virtually prohibits tax-exempt financing for the small businessman. We urge Congress and the Small Business Committee to take whatever action is necessary to reverse the effect of Revenue Ruling 81-216.

RLP/tm

cc: Senator Huddleston

24th Floor, Capital Plaza Tower, Frankfort, Kentucky 40601 (502) 564-4554

APPENDIX B.—LETTERS RECEIVED BY CONGRESSMAN VIN WEBER FROM CONSTITUENTS IN RESPONSE TO HIS REQUEST FOR THEIR OPINIONS

VIN WEBER
6TH DISTRICT, MINNESOTA

COMMITTEE ON SCIENCE AND TECHNOLOGY

SUBCOMMITTEES:
ENERGY DEVELOPMENT AND APPLICATIONS
SCIENCE, RESEARCH, AND TECHNOLOGY

COMMITTEE ON SMALL BUSINESS

SUBCOMMITTEE:
TAX, ACCESS TO EQUITY CAPITAL, AND BUSINESS OPPORTUNITIES

ASSISTANT REGIONAL WHIP
REPUBLICAN POLICY COMMITTEE

Congreſs of the United States
House of Representatives
Washington, D.C. 20515

WASHINGTON OFFICE:
514 CANNON BUILDING
WASHINGTON, D.C. 20515
(202) 225-2331

LEONARD [illegible]
ADMINISTRATIVE ASSISTANT

DISTRICT OFFICES:
ROOM 135
720 ST. GERMAIN
ST. CLOUD, MINNESOTA 56301
(612) 252-7580

[illegible] COLLEGE DRIVE
MARSHALL, MINNESOTA 56258
(507) 532-9611

September 14, 1981

Dear :

The Small Business Subcommittee on Tax, Access to Equity Capital, and Business Opportunities, on which I serve, will be holding its second hearing on Job Creation and the Revitalization of Small Business on September 22. While I realize that time is short (the hearings were just announced a few days ago), I'd like to get your opinion as to the impact of interest rates on current small business practices.

This, in my opinion, is the biggest, and unfortunately one of the most complex problems facing small businessmen and farmers today. The witness list prepared by the Chairman of the committe, however, does not appear to address this aspect of small business revitalization. Therefore, if you would care to submit a short statement for inclusion in the hearing record regarding your personal experience with the impact of these interest rates on your business activity, I'd be more than happy to have it made part of the permanent record. I fully intend to have this issue thoroughly discussed during the proceedings, and grassroots statements from small businessmen such as yourself would make this discussion much more timely and effective.

In any event, if you'd care to do this, you can send your material to my Washington office address listed above-- I think anything up to 5 pages would be sufficient. I would certainly appreciate your involvement in this, and will look forward to working with you again in the future. If you have any questions or comments, please don't hesitate to contact me.

Sincerely,

Vin

VIN WEBER
Member of Congress

VW/jh/kgr

MSI
Insurance

Honorable Vin Weber
514 Cannon Building
Washington D.C. 20515

Sept. 9, 1981

Dear Congressman Weber;

In reply to your 9-14 letter, asking for my opinions as to the impact of interest rates on current small business practices, I submit the following.

I am a multiple-line insurance agent in a small Minnesota town of 3000 population. I have been an agent for 20 years. The high interest rates are having a serious ripple effect in my business.

1. Less new vehicles are being sold, thus less new auto policies, directly due to high interest rates.
2. Few new homes are being built, thus fewer Homeowners policies, again due to high interest rates.
3. Commercial policies while still in force, are way down in premium. Such policies prices are generated by gross sales, payroll and fleet. Since all building contractors aren't building (due to high interest rates) their sales, payrolls and fleet units are way down and so is their premium.
4. Life insurance sales are down because of higher rates paid on savings. Not only are persons not buying needed permanent life insurance, they are loaning their cash values/dividends at favorable rates, draining cash from the life companies.
5. Health insurance premiums are rising dramatically because of costs of doctor, hospitals and drugs. A lot of these higher costs are directly attributed to high interest rates (clinic - hospital additions, etc.).
6. In all lines of insurance, many people are going without protection because they don't have the money. Without auto insurance in a state where mandatory auto insurance is required; without health insurance for their families, without house insurance adequate to compensate their loss; without life insurance necessary for their family security. And every uninsured loss is paid by society. Welfare, Medicare, direct relief, friends, relatives, unpaid doctor/hospital costs. High interest rates and inflation are evil partners.

JAMES A. BURROUGHS
504 1st St./Princeton, Minnesota 55371/BUS: 389-1282 MPLS: 332-6051
Mutual Service Life Insurance Company/Mutual Service Casualty Insurance Company/Modern Service Insurance Company

MSI
Insurance

In general, the high rates have literally closed businesses, are forcing farmers into bankruptcy, and have tightened money supplies necessary to survive in the business world. They are making the poor even more destitute and the rich more wealthy. Those high rates postpone indefinetly or even scrap small business expansion that would generate new jobs and more taxes. Money is so tight, it is changing the very way people live. We "little people" cannot relate to the billions, we only know there is less left after the necessities, sometimes nothing at all. Many cannot pay even the necessities, therein is the catch-22 situation created by high interest. When they began to finance necessities at the higher rates, survival itself is a real and ever present threat. Unless the high interest rate "cancer" is removed, like it or not, we are heading for the biggest recession in the history of our country with violent consequences.

Respectfully,

Jim

Jim Burroughs

JAMES A. BURROUGHS
504 1st St./Princeton, Minnesota 55371/BUS: 389-1282 MPLS: 332-6051
Mutual Service Life Insurance Company/Mutual Service Casualty Insurance Company/Modern Service Insurance Company

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PHONE (605) 336-2083

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507 W. THIRD
YANKTON, SOUTH DAKOTA
57078
PHONE (605) 665-9441

September 15, 1981

Congressman Vin Weber
United States House of Representatives
Washington, D.C. 20551

Dear Congressman Weber:

I am enclosing a copy of a letter addressed to the Honorable Paul A. Volcker, Chairman of the Board of Governors of the Federal Reserve System.

Unless we have some relief within the next few days, I would hold that the entire economy of the United States is greatly imperiled.

I beg that you and your colleagues do something to influence Chairman Volcker and the Board of Governors to achieve their goals before killing the proverbial goose.

Yours very truly,

Paul J. Heles

PJH/jag

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Triple Seal Tank
Balls & Specialities
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Lau Power Humidifiers
National Fiberglass
Hoffman Heating Specialities
Gutter & Rain Goods
Bob Floats & Valves
Fram Furnace Filters
Water Main & Ftgs
American Water Main Valves
Red & White Valves
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Durastall
Trane Products
United Marble Tops
A. O. Smith Water Heaters
Auto Soft Water Cond
L. B. White Farm Heaters
Tub-Master-Products
Trion Air Cleaners

September 15, 1981

The Honorable Paul A. Volcker, Chairman,
Board of Governors, Federal Reserve System,
Washington, D.C. 20551

Dear Chairman Volcker:

We have no intention of making this a long letter. Because of the high interest rates and an absolute downturn in the construction trades, we have been forced to lay off one third of our employees; naturally our sales were commensurately affected.

The high interest rate policy of the Federal Reserve has not cured inflation and I believe the continuation of this policy will result in a tragic overkill and I'm afraid the U. S. economy will be the victim.

Our economy needs an immediate revitalization and it appears that the first step would be an immediate and drastic reduction in the so-called "PRIME RATE". If there is a sensible and patriotic defense for the actions of the Federal Reserve System since your tenure, I would certainly be interested in the reasoning behind this high interest rate policy and the time frame involved in said action.

Yours very truly,

Paul J. Heles

PJH/jag

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BUTLER

September 16, 1981

Congress of the United States
House of Representatives
Washington, D.C. 20515

Dear Congressman Weber:

The high interest rates that we have today are ruining many small businessmen in our area.

Probably the hardest hit on the list are small Bldg. Contractors Implement Dealers, Automobile Dealers, and many other business people in general.

It is almost impossible to get any kind of long term Real Estate loan.

If anything were available it would be at a 20% or more interest rate.

An average new home in our area would be about $70,000.00.

In most cases the average working people do not have the down-payment for a home but assuming that they had $10,000.00 downpayment leaving a balance of $60,000.00 to finance the monthly payment for 20 years at 20% interest would be $1,019.30 per month.

A reasonable 10% interest for 20 years on the same home would be $579.02 per month.

This should indicate to any one in Washington what high interest rates are doing to small business in the rural area.

My guess would be if interest rates stay at present levels for one more year at least half of the small contractors, Implement Dealers, etc. will be out of business.

Sincerely,

Earl Raske

Earl Raske
Cosmos, MN

ER:lr

Fort Mille Lacs Village

MILLE LACS LAKE
Onamia, Minnesota 56359
Phone (612) 532-3651

September 16, 1981

Honorable Vin Weber
House of Representatives
514 Cannon Building
Washington, D. C.

Dear Congressman Weber:

Your letter of September 14th addresses a matter which is the most serious concern of most small businesses and particularly new small business.

Tax reductions are desirable but are only valuable to established businesses and those already earning significant taxable income.

Many small businesses and new businesses can not now benefit and may not survive to benefit or for that matter may never start at all if investment funds and credit are not made available in a more convenient manner and at lower rates.

New business and expanded small businesses are the nations greatest creator of new jobs and job training.

I should like to suggest as follows, an inovative government action that would greatly benefit that portion of the economy. I suggest that new and expanding small businesses be exempt or recompensated for the employers share of Workmans Compensation and Social Security on new and added employees and that an interest adjustment payment be made from the government based on the amount of added employment that was created.This act of government would greatly aid small business and new business to attract equity and survive in this high interest climate.

The serious decline in the resort and tourist related business in your district are but one example of the disasterious effects created by our present money market.

I have not tried to discuss our own particular problems because I am sure it is very similar to the hundreds of others you have heard. Enclosed is an article from this weeks local paper that treats with our tourist economy.

Sincerely yours,

S. A. Holbert

Enclosure
SAH:bgw

Franklin State Bank

1618
Members of F.D.I.C.
Franklin, Minnesota 55333

September 16, 1981

HONORABLE VIN WEBER
514 CANNON BUILDING
WASHINGTON, D.C. 20515

SMALL BUSINESS SUBCOMMITTEE

MY OPINION:

In addressing the issue of Tax and Interest for small business businesses in our rual communities, I feel that interest rates have a great deal of influence in showing down the economy.

If interest rates paid to the already wealthy could be lowered to allow a lower rate to borrower a more favorable rate, the farmer and small business man could expand and create more emplyment for auto and machine companies which in trun would generate more sales tax for the state and more income tax for federal government.

Interest rates paid should have a ceiling on savings of about 10% which in turn would decrease interest rate which would have to be paid to 13 ot 13½%, I feel assured the economy would be spurred.

Respectfully Submitted:

V.S. Sather, Pres.
Franklin State Bank
Franklin, Minn. 55333

Phone 532-4439
532-4840

SWesta BUILDERS, INC.
Box 318 - Marshall, Minnesota 56258

September 17th, 1981

Mr. Vin Weber
514 Cannon Building
Washington, DC 20515

Mr. Weber,

I am not into politics heavily, but I am into debt! Costs of doing business today with interest rates at 18 - 20% have changed my Company's basic way of doing business. I've enjoyed starting my Construction business 7 years ago, reasonable work with reasonable profits, minimal debt and when borrowing was necessary the interest rates were also reasonable.

Most small companys that I know must rely on the availability of Bank funds to grow. In addition, no Owner wants to stand still or go in reverse. We need growth and profits. A small Construction Company like mine requires certain lines of credit to get the necessary bonding to just be able to bid, not negotiate, the work.

With times and work as tough as it is, the high interest rate merely adds another shell in the chamber as we flirt with a daily game of Russian Roulette.

Thank you for your interest and efforts.

Regards,

Clifford J. Dahm, Jr.
President

BEDFORD INDUSTRIES, INC.
TELEPHONE 376-4136 AREA CODE 507
1659 ROWE AVENUE P.O. BOX F
WORTHINGTON, MINNESOTA 56187

September 17, 1981

Mr. Vin Weber
6th District Congressman, Minnesota
514 Cannon Building
Washington, D.C. 20515

Dear Mr. Weber:

Small business and high interest rates are a much talked about topic. The problem continues to drift along with everyone feeling that we are caught up in an avalanche and there's nothing we can do about it. Much like the energy prices that we were forced to swallow. It hurts but life must go on.

Our company is planning an expansion now, inspite of the interest rates, but the interest cost is an awesome expense to have to overcome. Because of these rates, one also has to live with ever changing rates throughout the term of the loan making it very difficult to price and sell profitably.

I feel less government in our lives is a step we all need to take. The thing I am concerned about is, can the small entity survive the time frame it will take to let supply and demand once again be our governing guideline.

I appreciate your flow of information.

Yours truly,

BEDFORD INDUSTRIES, INC.

Robert Boushek

Robert E. Boushek
General Manager

REB/acr

EST. 1935 PHONE 372-2131

Worthington Federal Savings and Loan Assn.

418 ELEVENTH ST. BOX 391 WORTHINGTON, MINNESOTA 56187

September 17, 1981

Congressman Vin Weber
514 Cannon Building
Washington, D.C. 20515

RE: Hearing on September 22
Impact of Interest Rates

Dear Mr. Weber:

First of all, Thank you very much for meeting in private with 3 of my board memebers - - - concerning high interest rates and what they are doing to the savings and loan industry - - - on your last visit to Worthington. I am sorry that I couldn't be there as I was attending our state leagues annual convention.

Somehow, we've got to get across that high interest rates do not control inflation, but that high interest rates actually contribute to inflation. As long as the Administration and Mr. Volker of the Federal Reserve permit interest rates to be kept artificially high as their method of fighting inflation, we will continue "bleeding".

The attitude of Treasury Secretary Donald Regan has been to let the savings and loans fail or merge if they cannot economically keep up. This attitude must be changed.

In other words, the Treasury Department and Donald Regan is our biggest problem. Their attitutde toward the savings and loan industry is not a good attitude. They are insisting on rapid de-regulation of our industry in a period of extremely high interest rates. (the worst possible time)

The savings and loan industry has been taken for granted by the administration and further, the committment to housing is not present in the administration

High interest rates have become public enemy #1 and the Administration and the Federal Reserve must let interest rates come down and fall to their natural level. Above all, this must happen.

Please tell our story at this hearing.

Sincerely,

John S. Remme

John S. Remme, President

JSR: jd

cc: Mr. Raymond Mork - Mr. Hardy Rickbeil - Mr. Roger D. Rohrer

MONTEVIDEO IMPLEMENT COMPANY TELEPHONE 1-612 - 269-6655 MONTEVIDEO, MINNESOTA 56265

"YOUR ALLIS-CHALMERS DEALER"

September 17, 1981

Honorable Vin Weber
Congress of the United States
House of Representatives
Washington, D.C. 20515

Dear Mr. Weber,

Thank you for your letter of September 14th, inviting my comments on the impact of interest rates for small business practices. The current high interest rates are really killing the small business operations as well as the farmer. Sales on major farm implements have fallen due to the high interest rates. Our business must also pay the banks 18%-20% interest on money we need for operating capital, which is most devastating to our business.

Immediate action must be taken to lower these interest rates, if we are to maintain our farms and small business operations.

Sincerely yours,
MONTEVIDEO IMPLEMENT COMPANY

William E. Homan, Owner

WEH/cb William E Homan

September 17, 1981

Honorable Vin Weber
514 Cannon Building
Washington, D.C. 20515

Dear Sir,

In response to your letter of 14 September concerning the effect of interest rates on current small business practices, I would like to offer the following comments.

Undoubtedly, this issue is one of the biggest and most complex problems small businesses face today. The current high interest rates make it virtually impossible for a business to obtain loans with any hope of investing the money in such a manner as to make a reasonable return on it. The problem is that between taxes (which are being taken care of to some extent with the recent passage of the tax bill) and interest, too much of the income from any business venture is taken out of the hands of the small businessman and he is left with little to show for his efforts.

As a result of high interest rates, it is extremely difficult in most cases to convince a lending institution that repayment of a loan can be accomplished if the borrower does not already have considerable income from an ongoing business. Consequently, the small businessman most generally cannot borrow the money he needs to make an expansion or to hire additional personnel. In some cases even badly needed replacement equipment simply cannot be obtained. In summary, the existence of high interest rates makes it impossible for small business to expand. Even survival is sometimes questionable.

The solution to the problem may lie in an approach similar to the savings certificates which will be issued shortly. Money raised through that type of a program could be earmarked for small business loans at a considerable reduction in interest rates from present levels. Unfortunately, limitations may have to be placed on the size of the business to which such loans could be granted although, if sufficient funds are accumulated, the ceiling could be raised.

Thank you for maintaining a high level of communications with your constituents. It is greatly appreciated and is a considerable change from what we have experienced with most of the past Congressmen.

Sincerely,

Harold R. King

Harold R. King, Ph.D.
1204 27th St. N.W.
Willmar, MN 56201

HK:ek

KANE TRANSPORT, Inc.

P. O. BOX 126
SAUK CENTRE, MINN. 56378

PETROLEUM COMMON
CARRIER &
GENERAL TRANSPORTATION

TEL. 612-352-2762
OR 612-352-2464

September 17, 1981

Vin Weber
Congress of the United States
House of Representatives
Washington, D.C. 20515

Dear Representative Weber:

The increasimg demand for truck transportation services in Minnesota and through out the upper midwest agriculture area prompts me to write this letter concerning the financial health of small businessmen in the truck transportation industry.

The truck transport business is a highly capital intensive business. Therefore interest rates, taxes and regulation are of great concern to us.

For small truck transportation businessmen the high interest rate, high rates of taxation and the burden to comply with regulations of NHTSA, DOT, ICC, and OSHA are devastating.

Capital for updating equipment and for growth must be financed at extremely high interest rates. Therefore making it nearly impossible to stay a viable and profitable business. Presently what little capital improvements we make are cash transactions. We cannot afford to pay interest rates at present levels and be a profitable business.

In the past we have bought used equipment for growth and replacement, which kept the total amount to be financed minimal. Therefore interest rates were not a burden. Now with higher interest rates even used equipment is out of the question.

If and when interest rates are withim our grasp we have an ambitous program outlined to up date our equipment and to expand. Thus taking advantage of current changes made in Interstate Commerce Regs.

Relief from high interest rates, high taxes and government regulation will again make small businessmen in the trucking industry competitive and a force in the truck transportation market place. With out this relief we will cease to exsist.

Sincerely Yours,

Tom Kane

Tom Kane
Kane Transport Inc.

TELEVISION
Service Center
PHONE 507-376-4322
708 TENTH STREET
WORTHINGTON, MINNESOTA 56187

Dear Mr Webber;

In Reference to your letter of Sept/14/81 asking about the impact of Interest Rates on Small Business. Let me just say this it Certainly hasn't been a help. however in my particular business there has been little effect. the tax cuts & lower inflation have been a help. to take up the increase in overhead by high interest, large ticket sales are suffering the most because many are purchased on contract & few financial institutions are interested in small sales contracts any more

Sincerely

Roger Bode

P.S. I would be interested to know what position you take on H.R 1454 Civil Rights amendment act of 81

MEMBER
PIA
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WORTHINGTON, MINNESOTA 56187

MEMBER
YOUR Independent Insurance AGENT
TELEPHONE
507-376-4171

September 17, 1981

The Honorable Vin Weber
514 Cannon Building
Washington, D.C. 20515

Dear Sir:

I received your letter this morning relative to interest effects on small business revitalization.

In the history of our country, the economy has never survived beyond 10 percent interest. Now suddenly we find our government insisting on 20 percent interest. The effects of this interest rate are crippling beyond your imagination. I am appalled that one man, Paul Volcker, has the sole power of determining an interest rate that can bankrupt half of the businesses and farmers in our nation. I agree that a reversal of prior trends is desirable, but we cannot undo 50 years of liberal thinking in one year's time. This process has to be gradual to prevent a total depression.

In our town there are practically no new businesses with the chance of success, little or no construction of housing or business buildings, and the economy is at a total standstill. If Mr. Volcker thinks that the average citizen in this area is on a spending spree, he is totally uninformed. Most of us are struggling to pay high gas and fuel bills, grocery bills and rental or housing payments each month. It is no longer a matter of trying to gain something, but more a matter of survival. Surely the Congress of the United States can do something to prevent Mr. Volcker from completely ruining the economy of our nation and of the world.

We are in the insurance and real estate business. Real estate cannot be sold because no one can afford 18, 19, or 20 percent interest. Insurance customers are coming in daily saying that we must reduce premiums in order for them to survive. If we are to continue in business, this trend must be reversed.

I appreciate this opportunity to express my feelings on the subject, and hope that it will help at your hearing.

Very truly yours,

Wallace Verdugt

Wallace Verdugt

WV:ct

Meyer Realty
1400 S. W. Trott
Willmar, Minnesota 56201

FLORENCE A. LORINSER — Broker

Sept. 17, 1981

Hon. Vin Weber
514 Cannon Building
Washington, D. C. 20515

Dear Congressman Weber:

Thank you for your letter of the 14th regarding the interest rates. Certainly these high interest rates have hurt all small business men and have hurt the nation as a whole.

My business, Real Estate, has been hurt even more---in fact has put it almost at a standstill. I realize that home prices were at run-away-inflation rates and I feel that prices should and are coming down. However, the average potential buyer in the West Central Minnesota area cannot afford to buy a home even if the seller reduces his price considerably if the interest rate is 16% or more. The incomes for average people in this area make this an impossibility.

The Farmers Home Administration is the only place that has made loans available to the average working class of people in this area and at this writing they are out of funds.

Bankers in our area say they have to loan with a 3 year balloon. This again does not make for a safe loan for the average buyer.

For sure, Big business will not flourish if the small business man is forced out of business.

I wish you success in your work on this subcommittee. Your job is not an easy one, but again I remind you, we depend on you-------You depend on us, and we are asking for relief from these high interest rates.

Thank you in advance.

Florence A. Lorinser

Florence A. Lorinser
Meyer Realty
1400 W. Trott
Willmar, Minn.

CLIPPERS' TEXACO
Verdi, Minnesota 56179 — Phone: (507) 368-9232

Sept. 17, 1981

Vin Weber
Washington D.C.

Dear Congressman:

I am also very mach concired about the high intrest rates.

I am in the Petroleum business, paying 18½ % interest on money I barrow. How are business men and farmers going to make ends meet at this rate.

Would appreciate any thing you can do to help get our intrest rates down.

Sincerly
G. Keith Clipper
of Clipper Oil Co
Verdi, Minn
56179

Tri - State Silo
and Equipment Co.

PHONE 348-3852 JASPER, MINNESOTA 56144

Sept. 17, 1981

Rep. Vin Weber
Congress of the United States
House of Representatives
Washington. D.C. 20515

Dear Rep. Weber,

I'm writing in respone to your letter of Sept 14, regarding the Small Business Subcommittee hearing.

I definitly know that high interest rates are affecting our business, along with the high cost of fuel and equipment for the farmer. The margins of profit for the grain farmer and livestockman have been erased - imagine having to take out 20% out of profit column on money borrowed, (especilly for the younger operator who borrows heavily) and try to keep from going bankrupt, much less make a profit.

The interest rate is forcing many farmers and small business out this fall, and if it continues, will certainly force many more on the welfare rolls.

It is causing people with money to invest in the money market, rather than create new jobs and businesses.

Agriculture and small businesses are the backbone of

S. DAK. MINN. Jasper IOWA

Tri - State Silo
and Equipment Co.

PHONE 348-3852 JASPER, MINNESOTA 56144

the nation, and if the climate continues to be bad for them, unemployment and strife will certainly ruin it.

I'm enclosing a clipping from today's paper, which is one of many Small Business in Trouble.

Sincerely
Holger Ausen

Economy, high interest rates force Jefferis to close

Rich Jefferis said it was a combination of high interest rates, his firm's recent entry into the Pipestone marketplace, and the drought and hail that hurt the county farm economy which forced his farm equipment dealership to close.

The dealership, which opened in January of 1978, closed its doors late last month.

"The combination of those things just kind of drains your capital funds."

The closing leaves the city with three major-line implement dealers. Jefferis sold the Allis-Chalmers line.

There are several other Allis-Chalmers dealers in the area, including those at Tyler, Westbrook, Luverne, Sioux Falls and Brookings. "But they've all been in business longer," said Jefferis.

"Just after we started we had the hail one year, then the drought, and the high interest rates. It gangs up on a person. I think a lot of businesses are in the same boat.

"I think the only thing that keeps some businesses going is that they have been in business for awhile."

Jefferis at one time employed nine persons.

"I do wish to thank the people that tried to keep me in business over the years," he said.

Jefferis has no definite plans for the future. "We're just looking around now."

The building, located at the intersection of Highway 75 and 30 South, has not been sold.

TRAUT WELLS, INC. Route 4 • St. Cloud, Minnesota 56301 • Telephone (612) 251-5090

September 17, 1981

Vin Weber
514 Cannon Building
Washington, DC 20515

Dear Vin:

I want to thank you for your concern involving high interest rates and small business. I'll try to organize my thoughts as best I can however, difficult with the short time I have.

To appreciate the problem we must go back to the mid 70's when we had a fairly stable economy. We, small bussinessman, proceeded in a normal course of business by borrowing money and buying equipment to preform our occupations. With reasonable interest rates we made jobs, people made money and of course payed taxes.

This cycle soon stoped with Volker's mad scheme of limiting the money supply. Of all the avenues available to limit inflation, high interest rates have certainly proved to be most ineffective. High interest rates effect all of us adversly in several respects. First off directly from the rates we pay to try and stay in business. Second the high rates government pays has to be picked up by business and some people in the end. Also we all help pay for the business failures due to high interest rates.

In the first quarter of 1980 over 300,000 bankruptcys were registered in the nation, of these over 40% were classified small business. The Carter administration,noted for its opposition to small business,dealt the final blow to us with Volkers and his suicidal program.

You may say, Well get out! That's quite impossible as our $250,000.00 machines are now worth less than twenty five cents on the dollar. Without work we have no place to go. High interest rates have reduced housing and construction to an almost standstill. For example we paid $55,000.00 interest in 1976 with a business volume of $2,000,000.00. This year we will pay over $160,000.00 interest on $2,500,000.00 volume.

High interest rates have proven totaly ineffective in controlling inflation. The present budget deficets are just the tip of the ice berg. The lack of productive people paying taxes will not even be the major problem coming up. These two problems will be multiplied by people like myself filing for tax refunds due to losses incured in our business. Example in 1976 our company paid $44,767 in federal taxes, in 1980 we filed for a loss & return of $244,50.

TRAUT WELLS, INC. Route 4 • St. Cloud, Minnesota 56301 • Telephone (612) 251-5090

The facts are that high interest rates profit only the rich, and will and are bringing total ruin to the economy and our country. The small business in this nation cannot hold out any longer, interest rates must be brought down even regulated if that is what it will take.

Thank you for your consideration.

Sincerely,

Marv B. Traut

Marvin Traut
President

PleasureLand, Inc.

37TH AVENUE & DIVISION STREET
ST. CLOUD, MINNESOTA - 56301 - PHONE (612) 251-7588

September 17, 1981

Congressman Vin Weber
514 Cannon Building
Washington, D.C. 20515

Dear Vin:

We have your letter of 14 September regarding the impact of high interest rates on our business.

During the year of 1980, high interest rates were the major cause of the largest and only loss that we have had in ten years.

The losses were so substantial that had we not had individual funds to inject into the business, we would have failed.

As our letterhead indicates, we are in the recreational business. We normally carry at peak, about one million in lot stock which we were forced to trim to about half that amount.

Because we guaranteed our retail paper, we have been accustomed to participating in dealer reserve. That was reduced to almost nothing. Normally that would have been about $40,000.00. Retail paper became almost impossible to handle. For example, a $20,000.00 contract would cost the customer, on a five year contract, about $10,000.00.

Our business for the year of 1980 was down over one million dollars.

We were forced to reduce the number of employees and cut our operation in every area.

A continuation of these rates strangles us to the point that we don't know how long we will be able to survive.

Congressman Vin Weber
514 Cannon Building
Washington, D.C. 20515

September 17, 1981

We have cut in every area that we can, but our fixed expense continues to climb, such as, light, heat, taxes, insurance, telephone, salaries.

Vin, we've been in business in St. Cloud since 1956, that's twenty-five years, and for the first time, we are hanging by our fingernails.

A continuation of having to live with these rates will mean our demise and the demise of a great many others like ourselves.

I guess all we can say is, "HELP".

Respectfully yours,

John M Pearson

John M. Pearson
President

Communication Concepts

P.O. BOX 132 • ST. CLOUD, MN 56301 • (612) 259-0910

September 17, 1981

Congressman Vin Weber
514 Cannon Building
Washington, D.C. 20515

Dear Congressman Weber:

Thank you for your invitation to me as a business owner to express my thoughts for the record of September 22, as part of the second hearing on Job Creation and the Revitalization of Small Business.

As a business owner and manager, I am being hard hit by high interest rates; they are my number one worry now.

For example, I would like to expand my business by making capital outlays for equipment, but high interest rates stop me from buying word processing macinery to make my business grow.

I note with concern the view of Dr. Henry Kaufman, as he was quoted in the Sept. 21 issue of Newsweek magazine. Kaufman predicts higher interest rates in the next six to nine months. Many other Wall Street brokers are pessimistic about the economic future also.

I am no economic expert, but I do know that tax cuts coupled with deficit federal spending can only spur higher interest rates.

I propose that you and other congressional leaders fight for deeper cuts in federal military spending; the $13 billion cut is not enough, in my opinion. I believe there is still much fat in the military budget; that is where the cuts should come now. I certainly do not want to see Social Security benefits cut or poor people harrassed any more by further government cuts in their direction.

One military cut that could be made immediately, in my view, is the recall of the El Salvador military advisors. It angers me to see the U.S. involving itself in the affairs of a South American country going through civil war; it is all too reminiscent of Vietnam. I am certain Secretary Weinberger can find many other ways to cut large amounts of money from his department without jeopardizing our defense security.

Sharon Deane Lesikar
President

As I indicated to you in a questionnaire you sent me earlier this year, I have supported Reagon's cuts in the federal budget, and I continue to support more budget cuts.

It does strike me as unrealistic, however, to expect Wall Street brokers to adopt Reagon's economic policies as they have been developed thus far. I, for one, am happy to see Wall Street following its business sense and not hopping on Reagon's bandwagon. The tax cuts passed earlier this year must be balanced by sufficient cuts in spending to justify them; anything less is irresponsible.

On November 13 I will travel to St. Paul as an elected delegate from St. Cloud to the Minnesota Conference on Small Business. I hope by that time to have seen positive steps by you and others in Congress to cut federal spending further in the military.

Sincerely,

Sharon Deane Lesikar

Sharon Deane Lesikar

SDL/eh

Oftedahl Drug
205 Sixth Avenue
Madison, Minnesota 56256

Richard Oftedahl
Reg. Pharmacist
Store 598-3864
Home 598-3260

Sept 17, 1981

The Honorable Vin Weber
U. S. House of Representatives
Washington, D.C.

Dear Mr. Weber:

Thank you for the opportunity to voice my views on interest rates and their effects on the small businessman and farmer...

In my opinion, interest rates are going to destroy the small businessman and farmer-Period!! I express this concern because of what inflation is doing to the small businessman and farmer...First of all most businesses use credit in their business because inflation has driven the cost of all replacement inventory up...This in effect has taken all of the profit dollars that would normallly be used to pay taxes and profit out of the business...The money that would be normally be earned is used to replace inventory and increased cost such as insurance, fuel costs, and operating costs...The business should show a profit and because it did the IRS wants you to also pay..Usually the money is in inventory so businesses have to borrow money to pay taxes...With current rates of interest your interest total is eroding your profit dollars.....

If the businessman and farmer had all sorts of money laying around he could get by but that is not

Oftedahl Drug
205 Sixth Avenue
Madison, Minnesota 56256

Richard Oftedahl
Reg. Pharmacist

Store 598-3864
Home 598-3260

even reality...Businessman don't borrow money because they like to but because they are now forced to...If you don't borrow you don't replace your inventory and with out inventory you don't have a business and that means no jobs...
The cost of interest is then added into the cost of doing business and prices have to rise...
Normal consumption is capitolism and tampering with interest rates to control the economy is not going to work..The governorment can regulate the small businessman out of business but rememeber we provide 54% of all the jobs....
How can this be corrected? I feel one of two ways or a combination of both...First reduce interest rates and get the economy moving...Let the market place work!! Second..All businesses need some type of inflation index built into their business to allow them to expand their inventories at the present level without being forced to pay taxes also on that inventory...example ...If the business starts out with a thousand units on hand it should not be penalized to maintain that level number of units...
Anything above that level would be..In retail businesses this could be a flat accross the board percentage...
Drug STore News in their summer issue stated that " for the first time every chains stores had

Richard Oftedahl
Reg. Pharmacist
Store 598-3864
Home 598-3260

Oftedahl Drug
205 Sixth Avenue
Madison, Minnesota 56256

showed declines in profit in spite of sales that had exceed the inflation rate.. No longer can chains depend upon increase sales to maintain profits".

The businessman and farmer have tradiontily used credit to help them further their business and farms to make them profitable; This is no longer true.. Unless interest rates are reduced you may find even greater problems-loss of more than noraml business' and farms...

Thank you for letting me express my views and I hope they will be of some help...

Sincerely,

Richard C Oftedahl

Richard C. Oftedahl R. Ph.
President
Oftedahl Drug
Madison, MN.56256

Sept 17, 1981

Congressman Weber:

My brother and I started our business in January 1973 when we purchased the Farm Equipment Dealership from our employer. Since that time we have expanded it from about a $500,000. business with five employees to a million and a half sales volume with eleven employees. During the earlier years of ownership the business did quite well due to a good economy which promoted good sales. Expenses seemed to be more in line with profits we were able to make on machine sales.

In recent years, the interest rates being raised by the Federal Reserve Bank have destroyed the working relationship between buyer and seller. Instead of high interest curbing inflation, in the farm machinery business, it is feeding it "rapid fire". Whereas the manufacturer is paying more interest on inventories before they are sold. Now, due to higher rates they are having to raise their prices to offset this extra expense. The higher prices are causing the buyer to be more reluctant in making that machine purchase, partly because he does not have the cash flow due to his higher interest rates. In some cases the farmer, who has the money for equipment purchases, will choose instead to invest his money in banks or loan companies and take advantage of this more sure form of profit, thereby keeping that money out of the machinery market.

Another side affect of this high interest on our business is that if we are going to sell equipment we must have it in stock. This stock is very expensive to maintain, particularly with these very high interest rates. Since competitive dealers get into the same trouble by slow sales on this inventory, they start to cut profit margins in efforts to move equipment costing them interest. When the profit margin is cut and expenses are already up, the business will begin to suffer. If a business cannot maintain sales and profits it will be forced to lay off employees and operate at a lower profile or if the situation keeps getting worse, close down.

I can see no way that high interest rates are slowing inflation or helping business in any way. Please do what you can to get rates back to a reasonable level. If something is not done soon, many small businesses will fail.

Sincerely

Richard Freiler
Vice President
Lake Henry Implement Inc.
Route 3
Paynesville, Minnesota
56362

KUEHL MOTORS, Inc.
307 8th AVE. - HWY. 75
PHONE (612) 598-3146
MADISON, MINNESOTA 56256
Buick - Oldsmobile
Pontiac
CHEVROLET
Sales - Service

9-17-81

Mr. Vin Weber

Thank you for the letter on Small Business Subcommittee on Tax, I appreciate your concern for the small businessman.

The high interest rates have had a terrible impact on my business. After working for 17 years as an auto Technician I bought my own Dealership in May of 1979.

at that time 'Floor plan' interest was 12% or about $\$80^{00}$ per month for a full size car. By the end of 1979 Interest per month on the car was $\$133^{00}$ at 20%. With the rising costs of cars and the high interest I have to cut back in inventory. at '82 car prices and current interest my per month car interest will be $\$166^{00}$ or double of 2 years ago.

KUEHL MOTORS, Inc.
307 8th AVE. - HWY. 75
PHONE (612) 598-3146
MADISON, MINNESOTA 56256

Buick - Oldsmobile
Pontiac
CHEVROLET
Sales - Service

This is also a result of GM raising car prices an average of $1,000.00 per year on full size cars (Who would expect any help from GM?) and GMAC raising floor plan costs to dealers (I would think 3/4 % over prime rate would have been enough) My average car * sales should be 180 units a year - but are only half of that. After losing $36,000.00 in my first year of business. Yes we need help.

KUEHL MOTORS, Inc.
307 8th AVE. - HWY. 75
PHONE (612) 598-3146
MADISON, MINNESOTA 56256

Buick - Oldsmobile
Pontiac
CHEVROLET
Sales - Service

I have laid two people off and my men are paid $12,000 per year. Not enough I know, but what can I do?

Thank you for listening Any and all help is greatly appreciated

Thank You
Wayne B Kuehl
pres

PCI
PROGRESSIVE CONTRACTORS INCORPORATED
8736 Zachary Lane • Osseo, Minnesota 55369 • Telephone: (612) 425-4515

September 17, 1981

Representative Vin Weber
House of Representatives
514 Cannon Building
Washington, D.C. 20515

REF: LETTER DATED 9/14/81

Dear Representative Weber:

My thoughts can be summarized very briefly; high interest rates are having a very large effect on our company's performance. We are a growth oriented company that demands a significant working capital loan. We are also a capital intensive company having substantial equipment investments resulting in heavy term indebtedness. High interest rates obviously add up to high cost factors. Where able(limited due to competition) we pass these costs on to the consumer - in our case, public agencies.

I do not believe, however, any sector of the economy ought to be given any relief over any other, or, for that matter, that any artificial restraints be put into the system. I understand the "Fed" does just that. But with the Administration working its influence, I feel it best to allow them the latitude they need to execute their program and trust it is the right one to stabilize our economy in the long term.

Sincerely,

Michael S. McGray
PROGRESSIVE CONTRACTORS, INC.

MSM:lmf

Bergerson-Caswell Inc.
GROUND WATER CONSULTANTS AND MEMBER OF
GROUND [illegible]

5115 Industrial Street
Maple Plain, Minnesota 55359
479-3121
Area Code 612

September 17, 1981

Congressman Vin Weber
514 Cannon Building
Washington, DC 20515

RE: Interest Rates

Dear Congressman Weber:

I don't need 5 pages - short and sweet.

Present interest rates are causing havoc with my business. Our cash flow is terrible, as our customers are working on our money - so we must go to the bank and borrow at 21% to keep the door open.

In the same breath, our business is very competitive and I must work on a 10 to 15% margin - but must pay 21% for money.

Everyone I talk to believes the high interest rates are causing inflation - I agree. Many small businesses are going to be forced out of business if the trend continues.

Respectfully,

BERGERSON-CASWELL INC.

Art Hart

A.R. Hart

ARH:mjh

WELL DRILLING AND REPAIRING BC **PUMP INSTALLATION AND SERVICE**
MUNICIPAL - INDUSTRIAL **DOMESTIC - ANY SIZE - ANY DEPTH**

UNITED FARM
REAL ESTATE —COAST TO COAST—

United Farm Agency, Inc.
Owen J. Baas
Representative
228 Georgetown Blvd.
Princeton, Minn. 55371
(612) Bus. 389-5851
Res. 369-4197

September 17, 1981

Vin Weber
6th District, Minnesota
514 Cannon Building
Washington, D.C. 20515

Dear Mr. Weber,

Your letter of Sept. 14, 1981 asked what effect interest rates had on my business. Because of interest increases I had to reduce inventory to the extent that profit turned to a loss. I have since started a second job (business) in an attempt to meet the needs of my family. The cost of money has literally destroyed my earning potential and changed my business from a tax paying to a red ink bottom line.

Thank you,

Owen Baas

Owen Baas

Keep up the good work Vin

• LAND • RESIDENTIAL • COMMERCIAL

CREATIVE HOME CONCEPTS, INC.
P.O. BOX 279 · ELK RIVER, MINNESOTA 55330 · TELEPHONE (612) 441-3754

September 17, 1981

Mr. Vin Weber
Congress of the United States
House of Representatives
514 Cannon Building
Washington, D.C. 20515

Dear Mr. Weber:

Creative Home Concepts, Inc. has been in the home building bussiness since 1972. My partner and I had accumulated a corporate net worth of $137,226.00 as of November 30, 1980. This net worth would no doubt have been larger if corporate taxes would have been lower. Because of this lower net worth our credit needs now are higher in a time when we can least afford them. However, the tax problem is no longer a factor due to high interest rates eliminating any profits that may have been taxed.

High interest rates have put the buyer out of reach of a new home. High interest rates have made it impossible for us to maintain an inventory that we can no longer sell. High interest rates have made it infeasible to borrow money to cover our operating expenses. High interest rates are destroying our equity and capital formation to a point that we will no longer be in bussiness in the very near future. It appears to me that unless you can do something about the high interest rates, other problems in this small bussiness will become irrelevant.

Sincerely,

Dale S. Nordby
Vice-Pres., Sec., Treas.

DSN:nmb

TRI-COUNTY State Bank

an independent bank

[illegible] P.O. BOX [illegible] ORTONVILLE, MINNESOTA 56278

September 17, 1981

The Honorable Vin Weber
Congressman, 6th District Minnesota
514 Cannon Building
Washington, D.C. 20515

Dear Sir,

The high current interest rates are having a very large negative impact on our business, a rural bank serving the local community. They have a much larger negative impact on the farmers, retail merchants, and small manufacturers. I do not subscribe, however, to the current hue and cry coming out of Washington, orchestrated by the news media. The present high interest rates are not a cause but a symptom of a problem. This problem was and still is inflation.

The Presidents economic program does not begin to take effect until October 1st, and yet the doom sayers started beating the drums against it in July. Congress is holding hearings that border on panic. Is it no wonder that investors get leary? Can congress stick to an anti-inflation plan? After 30 years or more of fiscal mismanagement, empty retoric, half truths from Washington, outright lies, and a policy of favoring consumption over investment, I believe investors will want to see some proof.

The regulations my industry lives under also increases the total cost to the borrower. Again, Congress has had a very large hand in creating an environment that has driven the interest rates to the highest peak ever. Banks and S & L were governed by Regulation Q which proscribed the rates paid to borrowers, now this regulation is being phased out to enable these industries to compete with the illegal money market mutual funds, which have competitive advantages without the restraints that we have. The depositors demand the highest rates and yet when or if they borrow, they complain at the high cost.

Liberal bankruptcy laws have added to the borrowers costs. Coupled with a judiciary that believes a promise to pay does not always really mean that.

I believe the time is long past for panicky quick fixes, for the band-aid approach to a very serious problem. This is a time for reasonable men to use reason. We must look down the road to build a solid base on which an economy can run well for all segments of society. We can not be panicked into the same mistakes that got us where we are today, even if it takes some bitter medicine to cure our ills.

From your past letters to me, congressman Weber, I believe you have the right ideas on the economy. I hope you stick to them and help to bring a reasoned patience to the deliberations.

Thank you.

T.H. Anderson

T.H. Anderson
President

TA/cl

MONTEVIDEO LUMBER COMPANY, INC.
PHONE (612) 269 - 9837
BOX 587 – WEST HIGHWAY 212 – MONTEVIDEO, MINNESOTA 56265

Sept. 17, 1981

Dear Congressman Weber,

Seeing we are in the lumber business we are very much aware of the high interest rates which are killing our small business.

People aren't building homes, they can't afford to with the high interest, but we still have to keep our shelfs stocked or close the doors, so we have to borrow and pay the high rate and hope it all works out.

Yours truly
Robert D. Bell

September 17, 1981

Congressman Vin Weber
House of Representatives
Washington DC. 20515

Dear Vin.

We have seen serious economic developments the past several years. I feel that government interference with the private enterprise system has added its toll to our economic problems.

In the past the small farm community was not immediately affected by prime interest rate fluctuation and government borrowings of funds; however since the "brainstorm" of Money Market 182-day and 2½ year Treasury Certificates of Deposits, the cost of funds has become a weekly dilemma for all financial institutions. The end result of this has been a near crisis for many financial institutions and the Small Business man who depends upon the local financial institution for his short and long term capital needs. The result of the aforementioned "High Cost Money" for financial institutions has created unbearable interest rates to the borrower, primarily the Small business man, farmers, and the consumer.

I realize however that we must provide incentives to save. Up until 10-1-82 (all savers certificates) our country has penalized the saver. I fully agree that we must continue to come up with good "common sence" ideas to encourage people to save.

Sincerely

Herb Rozkin
1430 Indian Hill Road
Worthington Minn 56187

STATE BANK of Edgerton
845 MAIN, P.O. BOX 427
EDGERTON, MINNESOTA 56128
PHONE 507/442-4061

A. J. EKDOM, Pres.
G. H. FRIEDELL, V. P.
L. G. BROUWER, V. P. & Cashier
A. E. ROMKEMA, Ass't. Cashier

September 17, 1981

Mr. Vin Weber, Congressman

Washington, D. C.

Dear Mr. Weber:

This is regarding your Small Business Subcommittee on Tax, etc, letter asking our opinion on high Interest Rates. The impact on high interest rates on current small business practices has been tough on them. Implement dealers are having a difficult time selling machinery and equipment and car dealers are unable to make enough sales to meet expenses.

It is especially hard on young farmers borrowing large amounts of money to make ends meet. I had one young farmer in yesterday saying he isn't able to keep ahead of expenses due to high interest rates. And this is the case with most of them.

Look what it is doing to some of the Savings and Loan Associations? I'm afraid the whole economy is going bankrupt.

However I am in agreement with Mr. Volcker that inflation must also be curbed. But in order to do this the government has to stop (spending) printing money to pay the bills. We can't keep this up forever. I think the burden is on Congress to make additional budget cuts to reassure financial markets. I think the outlook for interest rates is ultimately going to be determined by a market judgment as to how successfull the Federal/Reserve will be and how successful Congress is going to be and how successful the administration is going to be in using monetary and fiscal policies designed to attack inflation.

Even the people who do have substantial amounts of money to put on interest at the high rates say this isn't good.

Enclosed is a ABA opinion which you might get some additional information from.

Best Wishes and may you be instrumental in getting rates down and inflation and spending by the government down.

Sincerely,

A J Ekdom

President.

September 15, 1981 **A Supplement to Capital**

AMERICAN
BANKERS
ASSOCIATION

Perspective

● High interest rates are the big issue in Washington today. With the political roulette wheel whirling to decide where the blame for high interest rates will be assigned, the Sept. 11 Washington Post carried a refreshingly factual Q&A analysis, including the following:

> Q: Republican leaders in Congress claim high interest rates are basically the fault of Wall Street. What, if anything, can Wall Street do to bring down interest rates?
>
> A: Wall Street is just a catch-all phrase meaning financial markets. There is nothing that participants in the markets can "do" to bring down rates. However, if the supply of money increased or the demand for it fell, borrowers would be able to find lenders willing to lend at lower rates. This would happen not just in New York City, but in Washington and elsewhere, too.

But in spite of this and other calm explanations of the workings of financial markets, the simple fact is that Congress is in a panic over the voters' attitude toward the cost of money.

● No matter that none of President Reagan's bold initiatives even begin to take effect until Oct. 1. No matter that only gradual economic improvement has been forecast thereafter by the President and his aides. No matter that common sense says any economic turnaround takes many months, not days or weeks. No matter that the Administration is acting quickly to make additional spending cuts to hold down the federal deficit.

With members of Congress on both sides of the aisle uncertain as to how to proceed, the scenarios range from the uncomfortable to the appalling: much finger-pointing, but no action, as Democrats wait for public wrath over interest rates to descend on the White House; formation of study committees to focus the glare of publicity on banks, or the Administration, or both; attempts to enact a "windfall profits" tax on lenders who charge rates more than 6 percentage points over the inflation rate; attempts to invoke the 1969 Credit Control Act (as the previous Administration did, disastrously, in 1980); or perhaps other efforts to encroach on the Federal Reserve's independent management of monetary policy.

● Depositors, presumably, are or will be borrowers. The anomaly of today's situation is that depositors are forcing up the price of money feverishly -- yet rebel at the cost of money for loans.

With those deposit interest rates running at 16% plus for the most popular certificates, it's difficult to see how loan rates could be lower. In fact, with over $150 billion drawn from banks and other depositories into money market mutual funds over the past two years, it is remarkable that virtually all institutions have been able to continue fully serving their customers.

● But Congress has blood in its eye. As the representatives and senators reconvened last week, it was clear that for those on the firing line -- lenders --

(more)

the scenarios ranged from heavily negative public comment to efforts to impose credit controls. There is no strong political voice of opposition to this sentiment. In this atmosphere, logic and factual argument have little if any place. Some will vilify lenders, and others will push for credit allocation.

On a less hasty note, the House Banking Committee plans coast-to-coast "grassroots" hearings on interest rates stretching into December.

- The voice of reason says, give the Administration's program time to work. But the politicians may not be able to wait, and that inability to wait holds dangers. For a new program of credit controls or credit allocation at this time could sidetrack the Administration's opportunity to turn the economy around. Trust -- that slender thread -- built by the Reagan Administration could evaporate if credit controls were enacted. Without that trust, no economic plan can succeed.

- ABA President Lee E. Gunderson and ABA's Economic Advisory Committee have issued the following statement regarding interest rates:

"The American Bankers Association shares the concerns of the general public with respect to continuing near-record interest rates. But the ABA believes that policies designed to bring down these rates must look to a permanent and long-run solution, rather than any type of short-term quick fix.

"The current policy of the Federal Reserve to restrain the growth of the money supply is fundamentally correct. We are encouraged that the Administration continues to support the Federal Reserve in its resolve to meet its stated goals.

"We are also encouraged by the steadfast determination of the Administration to further restrain federal spending to ensure that budgetary goals for Fiscal Year 1982 and beyond are met. We give our full and active support to the additional efforts to reduce spending that are necessary if this nation is to have anti-inflationary fiscal policy as well as anti-inflationary monetary policy.

"A significant component of today's high interest rates is an 'uncertainty' factor. This is a direct result of the skepticism of the savers and investors across the country who have for 15 years watched as stop-and-go economic policies in Washington have created a tremendous inflationary momentum that has only now begun to abate. This is not a 'Wall Street' phenomenon or a vote of 'no confidence' in the economic policies of the current Administration. Rather it is the symptom of a long illness to which the medicine is just now being administered.

"The renewed calls for quick fixes to the high interest rate problem serve only to add to the 'uncertainty' factor. Credit controls, by their record of March, 1980, are a disproved remedy. Serious talk of credit controls is self-defeating because many corporate treasurers draw down their reserve lines of credit as a way to insure against such a development. This adds upward pressure on interest rates.

"There is widespread misunderstanding as to what will happen if the Federal Reserve succumbs to pressure and loosens its reins on the money supply. In today's environment, such an action will cause even higher interest rates, as savers and investors anticipate a new round of inflation.

"The return on equity of banks and other businesses has suffered as a consequence of the level and unpredictability of the future course of inflation. This has made it difficult for lenders to maintain a positive spread between the cost and price of their funds.

"The American Bankers Association has full confidence that the policies of further spending and monetary restraint are correct and necessary in order to restore long-term economic strength to this country. There is no other fundamentally sound and correct policy that we can follow. If we delay or vacillate in the implementation of these policies, there will be a need for a more painful administration of them later on. Only these long-range solutions will ensure an end to the steadily escalating cycle of inflation and high interest rates."

# \# \#

Hohn Implement Inc.
Adrian, Minn. 56110
Phone (507) 483-2838

Mr. Vin Weber
514 Cannon Building
Washington, D.C. 20515

Dear Mr. weber:

As we are all aware there are many factors which have culminated to put us into the ecomomic situation we are in now. On the agriculture end we are continually fighting low commodity prices, low livestock prices, and high equiptment prices;however these fluctuate enough that we can cope with them. High interest is beyond our means.

High interest is having a greater impact on our business than all the other factors put together. Large ticket item sales, which are our bread and butter, are virtually non-existent. Farmers will buy equiptment speculating on higher livestock and grain prices, but not with 20% interest staring them in the face.

High interest does absolutely nothing for a country. The person who has nothing and is trying to build for his future is only put further in debt. The person who has money to invest does not need to earn 20% interest on that money.

We, as a country, are trying to reach a balanced budget? This a very poor way to go about it. How many millions of dollars in revenue will the Gov't. loose this year due to the drop in personal and corporate incomes? How many millions of dollars is our GNP going to drop?

As the economy got weaker many people were to far in debt to adjust to the situation, so therefore were forced into bankruptcy. As we all know the only one who wins in a bankruptcy court is the debtor. He walks away with a clean slate and cash in his pocket; Meanwhile the creditor who took the man in good faith, is left holding the bill. which could ultimately, and has, put his business in financial difficultly.

Bankruptcy's have a direct connection with high interest and both are very damaging to small business.

Hohn Implement Inc.
Adrian, MN 56110
Phone (507) 483-2838

As far as I can see the Gov't. does not want to get the economy straightened out, or the wouldn't be offering 2½ yr. savings certificates at 10% plus interest. Anyone who can look ahead 2½ yr. and pay that rate of interest on savings is definitely holding all the cards in this game.

Until the gov't. decides they have destroyed enough business and households there will be no end to this pre-fabricated confussion.

Sincerely,

Dennis L Hohn
Hohn Imp. Inc.
Adrian, Minn. 56110

Park Tool Company

HYDRASPLIT

Post Office Box 188
Saint Cloud, Minnesota 56301
Phone: (612) 251-5077

September 17, 1981

Honorable Vin Weber
House of Representatives
Washington, D.C. 20515

Ref: Small Business Subcommittee on Tax, Access to Equity Capital and Business Opportunities

Dear Congressman Weber:

Your letter of September 14, 1981 was welcome and pleasant.

As you have said, the problems are complex and far reaching. It's hard to know just what to recommend or do.

Our business revolves about our customers as does every business. Some of our customers are involved in the construction industry, commercial and residential. The balance of our customers are in more stable line of business.

Since the construction industry has been slowed, we have concentrated on our other lines. Fortunately, we are in a position to capitalize on some new technology and our customers are eager to invest in our products (capital equipment). The tax changes should help more.

Over the last several years, we have been able to export some of our products to Europe and other countries. That is now more difficult with the strengthening of the dollar.

We are also experiencing some competition from European manufacturers in our U.S. market. Apparently, the European investment climate, in the past, must have been more favorable than ours as the European technology and the willingness to adapt it exceeds the U.S. conditions. In any case, we are playing "catch up" with European competitors here at a time when their product is cheaper and their financing costs lower.

PIONEERS IN STONE AND MASONRY CUTTING EQUIPMENT

High interest rates make business more difficult and to some extent, I believe, are inflationary since they do drive up costs. As you know, that's a complex consideration.

All things considered, however, the high interest rates may be the best route. As a businessman, I believe that any business venture should be profitable. We have seen lots of deals, the last few years, which are "unprofitable" operationally, profitable only in terms of tax considerations. In many, if not all cases, these investments are nonproductive drains on what could and should be true "working capital" of our economy. To some extent our capital has been used for luxuries or the necessities (energy, minerals, technology, defense) have gone begging.

The only way I see to correct this is to offer a more attractive package to the investor. Maybe that means a venture capital program that could pool funds under a "revenue bond" type program. The "programs" always seem to lead to abuses and special interests, however, so I'm not real excited about those either.

You know, Mr. Weber, while things are rather perplexing at this time and lots of folks are having trouble, generally speaking, most everyone is better off than they were 25 years ago.

We have come to have some very large expectations and demands, some of which are a bit ridiculous. Maybe we need to learn to examine our priorities and needs more carefully. Our current economy certainly promotes that!

Truthfully, I believe we're on the right track. American businessmen are problem solvers and they'll find a way to do it, better than the politician will! We must be patient and diligent but it can be done!

There is a lot I don't know about business, Mr. Weber, but it seems that the simplier it is, the easier it is. The only folks that gain from these "programs" are the ones who know how to take advantage of them. That excludes most of the entrepeneurs and innovators who don't have time or resources to study the programs.

As you can see, I'm not sure I understand the problem, let alone the solution. Hope you can make some sense from this. Thanks for asking.

Sincerely,

PARK TOOL COMPANY

Thomas L. Schlough

dk

9-18-81

After much contemplation I had contracted to convert my business from a manual to an automated process. Long range planning and contracts were involved.

The net result was that I had to pay the increased costs of money out of a reduced income (due to the economy) and I for the first time in business experienced serious financial problems.

In order to meet my financial obligations I had reduced my staff for 16 employees to Seven. This does not help me or the national economy.

It is an experience I never want to face again.

However, I am willing to sacrafice if everyone else is*

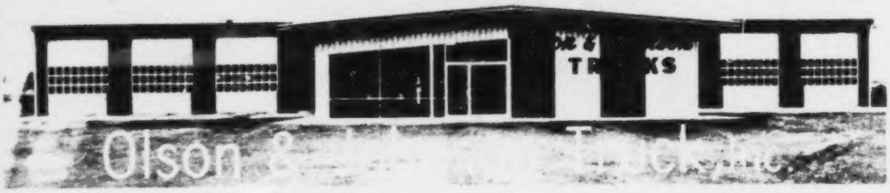
I contine to support you and the President in his budget cuts. WE ALL SIMPLY MUST CUT THE SPENDING.

Sincerely,

R. J. Egerman pres.

Credit Bureau of St. Cloud, Inc.
P. O. Box 99
St. Cloud, Minnesota 56301

Hiway 59 North Phone 532-5719 Marshall, Minn. 56258



9-18-81

The Honorable Vin Weber
6th District Representative

Dear Sir:

In your letter dated September 14, 1981 regarding the hearings to be held on September 22, 1981 for Job Creation and Revitalization of Small Businesses, I will attempt to respond very briefly.

I am a second generation owner of the business. I have just recently purchased the business from the previous owners. The interest rate on these purchases were driven up by the prevailing commercial rates. Our whole sales and service business depends on inventory on hand. If I would have the money to buy this inventory without borrowing or floor planning, I would not be in business, but instead clipping coupons on the money markets. The interest being earned by these people is coming out of my pocket and driving my business slowly to bankruptcy.

We used to employ about 24 persons and some parttime help. We now employ 18 and 1 parttime. If this is good for the job market and for small businesses like mine, then I have to change my thinking.

If the President thinks for one moment that a recovery is going to happen rapidly it would be the biggest mistake he makes. We have went backwards too long and too far in small business to expect us to rebound right back. We have a lot of catching up and healing to do before we can again start to go forward and expand.

Yours,

Arthur M. Olson

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WORTHINGTON, MN 56187

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September 18th, 1981

Honorable Congressman Vin Weber
514 Cannon Building
Washington, D.C. 20515

Dear Congressman Vin Weber:

I just received a copy of President John Remme's letter to you giving you a picture of our serious concerns in The Savings and Loan Banks.

He has stated our problem very well and hopefully you and your Committee can prevail on Donald Regan and the Administration to re-study and then act to relieve this serious high interest situation for Home Ownership that is hurting the entire way of life in our Country. * Many dreams of HOME OWNERSHIP have been side tracked and often completely given up. This must change and hopefully soon.

This is not a letter for the record, but just to you and pretty much off the cuff. Vin, we are very proud and pleased to have you representing us. Keep on with your thorough RESEARCHING--Analysing---Planning---and then Acting---and Following Thru. Please don't let this devasting HIGH INTEREST PROBLEM get shelved. Keep it on the front burner.

We are very optimistic for the future and as the inflation rate slowly comes down it is only logical that interest rates must slowly follow. From the very high point they are at now surely it is logical for Congress and The Treasury Department, The Federal Reserve, and the Administration to work together to help them keep on moderating. It seems to me we are seeing some downward movement right now. We know these many needed changes have numerous side effects that have to be given some time to work themselves out. There is a pent up demand for Housing, Automobiles, and most everything else that must be gradually satisfied, so changes of necessity must be gradually, but they must move down with interest rates as the inflation rate drops slowly. The increased demand will put more people back to work. Great progress has been made in the area of inflation and now Congress must create an economic climate that will put more of our people back to work. * Moderating interest rates will help to do this. Government, Capital, Labor, and Management must learn to work as a team and not always fight each other for what, quite often, is an unfair advantage.

Keep up your dedicated efforts for better Government decisions and leadership. If we can be of help at anytime, please call on us.

Please let us know what we can do to save the Saving and Loan Programs

Sincerely,
F. Hardy Rickbeil
F Hardy Rickbeil

No dictation here - so please excuse my errors.

Turkey Day was Great.

The Crops are beautiful and bountiful

EB
EMPIRE STATE BANK
COTTONWOOD, MINNESOTA 56229
Phone 507-423-6285

ADRIAN [illegible] GOLBERG
President
DOUGLAS ANDERSON
Vice President
MARK R. ELSTON
Assistant Vice President
MARK BJORNEBO
Assistant Vice President
RUTH POST
Cashier
JULIE BODE
Assistant Cashier

September 18, 1981

Honorable Congressman Vin Weber
U.S. House of Representatives
Congress of the United States
514 Cannon Building
Washington, D. C. 20515

Re: Letter of September 14, 1981

Dear Congressman Weber:

I have been following the rhetoric prior to and after the passing of the Tax Reform Act of 1981 and it is interesting to note how quickly solid reasoning has dissipated even among the soothsayers on Wall Street. Reagan's program is a quite satisfactory program which involves reducing the tax burden on the American people, encouraging people to save and invest, companies to revitalize their plant and equipment, and finally to obtain a strong dollar and a balanced budget. You must have realized as did I that it might hurt for a while, that business might be unable to adjust and the pain might cause greater bankruptcies, plant closings, unemployment, reductions in welfare costs, etc. When are the American people going to realize that in order to stop inflation which is a greater penalty to our future generations than anyone cares to admit.

The tight money position advocated by the Reagan Administration and the Federal Reserve is working to drive down the excess created over the past ten years. When people start to complain, it is an indication that the treatment is beginning to take effect and the patient is gradually going to improve. If we backtrack or retrench, we deserve to get beat at the election booth come next November or in 1984. What must occur is now to cut the budget as far as necessary to accomplish a reduction in the anticipated deficits due to the higher interest costs associated with the tax reduction program. Wall Street is now betting that Congress will accede to the wishes of the American people and loosen the reins on credit and interest rates so they can continue on their spending spree.

If we are committed to seeing this through, we must stand ready to accept the consequences. The problem as I see it is that the Fed has stood alone rather than having the approval of Congress to see that we start to cut programs and prune the fat which has developed through adding more and more governmental programs at every level of government. The money market funds have hurt banks and savings and loans tremendously at a time that they should have been controlled and this had made the job of the Federal Reserve Bank even more difficult. When the people find out that MMMF's don't make loans to farmers, businesses and individuals maybe they will think about where they are investing their money to the detriment of their community and area. Treasury Secretary Reagan and the Fed have done nothing to mitigate the problem other than adopting the philosophy of "Ignore it and maybe it will go away".

"LYON COUNTY'S LARGEST INDEPENDENT BANK"
INDEPENDENT COMMUNITY BANK

If you think that Paul Volcker and the Fed will loosen up on the interest rates without corresponding cuts by Congress in the budget, I think it is naive. I could give you many instances on how interest rates paid by the government on its borrowings have hurt our bank and its customers, but the U.S. must get its house in order before the American people will accept a philosophy of savings rather than spending, investment rather than consumption, stable economics rather than continued inflation, and more productivity rather than less.

Let us allow the American system to function on the supply and demand basis without letting the big banks swallow the little banks, banks buy the troubled savings and loans, stop the intrusion of mutual funds and non-financial institutions into traditional banking and disallow the continued buying up of American banks by foreign based companies or multi-national financial conglomerates. We must be prepared to assist troubled industries due to the rapid changes made by Congress and have regulators flexible enough to allow time for everyone to adapt to the different economic situations we find ourselves. The program will work and we'll all be better off for it. One suggestion I have is to eliminate the Depository Institutions Deregulations Committee as soon as possible. They have done more to confuse the situation and have added more inane regulations and laws which are contradictory with the purposes of the so-called Deregulation And Monetary Reform Act of 1980.

Keep at the purposes for which you were elected and don't forget the support given by those like myself who haven't responded promptly in defense of our plans. Thanks for the opportunity to express my concerns.

Sincerely,

Adrian C. Golberg

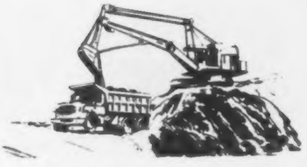
Adrian C. Golberg
President

P.S.

Enclosed are some items of interest which I have copied for your reading and received some of SBA's problem loan auction notices.

Winter Construction

Box 78 • [Office] 620 3rd Ave. S.E. • [507] 825-4696
[Shop] 420 3rd Ave. N.E. • [507] 825-3465
Pipestone, Minnesota 56164



September 18, 1981

Mr. Vin Weber
Minnesota Representative
514 Cannon Building
Washington, DC 20515

Dear Mr. Weber:

Your letter concerning interest rates arrived at a time when we have had to make many decisions regarding our financing, refinancing and equipment purchases. As a matter of fact, in some of these decisions there are no alternatives but to accept the 19% rate and hope that at the next renewal date there has been a beneficial decrease in rate.

Equipment purchases are at a standstill at this point in time and we have resigned ourselves to repairing our older machines until it is economically feasible to replace them. Leasing is an option that is available, however if you want to purchase the machine at a future date, the payments are applied to the purchase price, less a interest charge of 2-3% above prime. As you can see, this also strains cash flow and it is quite costly as far as interest is concerned.

1980 started a trend on our financial statements that I'm sure has been seen in other small businesses. The average cost of money for the year ended 12-31-80 was 14.81% for Winter Construction Company and 12.33% for Winter Concrete Products, an increase of 20.70% and 31.45% respectively over 1979. This is an uncontrollable cost to us in the sense that the money must be renewed and there is no substantial savings in "shopping around." How many businesses can weather another 20 - 30% increase in such an expense for 1981? We were fortunate enough to reduce our debt load going into 1981, yet the total expense for interest increased 12% for the year ended 1980. If we would not have been able to reduce our debt by 9.50%, our interest cost would have skyrocketed to an unbelievable and untollerable figure.

1981 is bringing us no good news and 1982 does not appear to be appealing either. With the construction industry bidding closer and closer to cost, there is hardly anyone who can bear any more substantial interest raises with such tight gross profit margins.

I hope this information is helpful to you and to your committee even though I couldn't elaborate more since time is short and I tryed to condense the information as much as possible without sacrificing the point to be made.

Yours truly,

William A. Winter, Owner
WINTER CONSTRUCTION &
WINTER CONCRETE PRODUCTS

WAW/kkh

NORTHERN WIRE PRODUCTS, INC.
WEST DIVISION STREET • P.O. BOX 70
ST. CLOUD, MINNESOTA 56302 • PHONE (612) 252-3442

Powder Coating
Vinyl, Nylon & Epoxy

Fabricators of Quality Wire Products
(SINCE 1959)

September 18, 1981

MR. VIN WEBER
720 St. Germain, Room 135
St. Cloud, MN 56301

Dear Vin:

In reference to high interest rates and the problems they create for small business, I would like to make the following statements.

It is extremely difficult for small business to pay from 18-25% interest and still continue to operate a viable business. It is also difficult to price your products not knowing what the interest rates might be tomorrow or next week and because lending institutions will no longer borrow at a set rate for long periods of time your interest costs fluctuate dramatically.

We, at Northern Wire, have virtually ceased to purchase any new equipment and facilities. We have cut back on all major expenditures that absolutely do not have to be taken care of at this particular time.

Our profits are lower than in the past year. Our business condition is not as good as it was a year ago nor as good as it was three months ago. At the present time we have several employees on lay-off status and other employees are working four day weeks instead of five.

We are spending money on advertising and other sales efforts that we feel is probably going to be wasted but we are trying to find enough business to continue operating at a level so we do not have to lay off or lose additional employees.

The problems we are having are no different than many small businesses and also large businesses are having and until the interest rates come down to a level closer to 12%, rather than 20%, I do not see our economy making the changes that are necessary.

Sincerely,
NORTHERN WIRE PRODUCTS INC
Merton Hubbard
MERTON HUBBARD
President

MH/bcl

Area Code 612/251-8450

united granite sales co.

505 17th Ave. North P. O. Box 844 St. Cloud, Minnesota 56301

September 18, 1981

Congressman Vin Weber
514 Cannon Building
Washington, D.C. 30515

Dear Vin:

Our company is quite small, employing 15 persons at present and was a partnership of my Father and I until 1955 when it became a Minnesota Corporation. We have been consistant employers in St. Cloud since my Father began in 1935.

Your concern regarding high interest rates is correct and appreciated. The interest rates at the level that has prevailed for the last several years, are depleting our cash reserves, inhibiting our ability to purchase properly, and of course, preventing capital and plant improvements.

The best long term rate (5 years) we could obtain at present for plant improvement is 18% which simply is not affordable.

Should this situation not turn around soon, we may not be in a position to recover financially.

I sincerely hope that you and your colleagues will find some way to improve this element of our economy.

Sincerely,

UNITED GRANITE SALES CO.

Robert P. Honer

Robert P. Honer, President

RPH/db

"WHERE QUALITY AND SERVICE ARE UNITED"

Culligan®
CULLIGAN WATER CONDITIONING, INC.
81 E. 12TH ST. WORTHINGTON, MINN. 56187 TELEPHONE: 376-4441

Mr. Vin Weber

I would like to tell you in this short letter what the high interest rate is doing to my business here in Worthington.

It is causing almost a 100% decline in house building, also it is making customers do without rather than buy and put a unit on timepay because they have payments that are not even in the ball park.

As I see it. if the interest does not drop soon, I might be forced to lay off an employee because of lack of Work.

Sincerely
Gary Oberloh
Culligan Water Cond.

Balaton Elevator Co.

Fritz Knochenmus, Manager

Box 66
Balaton, Minnesota 56115

Phones: Grain Dept.
734-5751
Feed Dept.
734-5851

HONORABLE VIN WEBER
CONGRESSMAN
WASHINGTON D.C.

DEAR SIR,

: REGARDING HIGH INTEREST AND HOW IT AFFECTS OUR BUSINESS AND AREA.

BEING THAT WE RUN A GRAIN ELEVATOR IN A RURAL AREA, DURING THE PEAK OF THE GRAIN SEASON , WE MUST BORROW MONEY TO OPERATE OUR BUSINESS AND AT 20 % ,YOU CAN SEE WHAT HAPPENS TO GRAIN MARGINS IF YOU NEED THIS EXTRA CAPITAL FOR ANY AMOUNT OF TIME. BUT I'M MORE CONCERNED ABOUT OUR AREA FARMERS, THEY HAVE TO BORROW MONEY TO GET THE CROP IN THE GROUND AND FOR THE FUEL AND SPRAYS TO KEEP THE FIELDS CLEAN AND CULTIVATE AND WHATEVER. ONE OF OUR FARMERS USED $ 14000.00 FOR BASIGRENE SPRAY FOR HIS SOYBEANS ALONE. THEN IF THEY HAVE THEIR GRAIN SEALED WITH C.C.C. THEY ARE PAYING 15% ON THAT MONEY AND 20% ON MONEY BORROWED FROM LENDING INSTITUTIONS. IF THEY ARE FEEDING CATTLE AND PAYING 20% FOR THE BUYING OF THESE CATTLE THE ONLY ONE WITH A CHANCE OF MAKING MONEY IS THE BANK. IT IS COSTING THE FARMERS A LOT MORE TO OPERATE, BUT AT THE SAME TIME HIGH INTEREST DEPRESSES THE VERY PRODUCTS THAT HE HAS TO SELL. MOST OF THESE FARMERS ARE GOOD OPERATORS BUT I DO NOT KNOW HOW THEY WILL SURVIVE UNDER THE PRESENT CONDITIONS.

YOURS TRULY,
Fritz Knochenmus
MANAGER-SEC.-TREASURER
BALATON ELEVATOR CO.
BOX 147
BALATON, MINN. 56115

September 18, 1981

**ANDERSON
CHEMICAL
COMPANY**

Honorable Vin Weber
Congress of the United States
House of Representatives
514 Cannon Building
Washington D.C. 20515

Dear Vin:

Thanks for asking my opinion on the matter of interest rate impact on small business. At $7,000,000 sales I don't know if we're still considered small but I'll comment anyway.

The problems which I have been witness to in Litchfield are not the same as Anderson Chemical Company faces. We are growing more profitable in the face of rising money costs. The reason is that our debt to equity ratio is about .15 and unlike many retail operations, we don't finance our accounts receivable or inventories from bank loans. All our debt is long-term and small.

I feel good about our financial stability but empathize with car dealerships which are paying 22% for floor plan financing. I know they are running red ink all over their showrooms, and I feel for them because of their plight.

Vin, can money supply be contracted via higher reserve requirements on banks and S & L's? I know the Monetary Control Act eased those requirements thus expanding the money supply through fractionalism.

The only other way to bring the money supply into check is by getting the deficit under control, thus eliminating the Fed from competing with private sector for financing. Maybe it will take a constitutional amendment or the gold standard to do that if Congress is unwilling to bite the bullet.

Most Respectfully,

ANDERSON CHEMICAL COMPANY

J. Terry Anderson

J. Terry Anderson
President

JTA:vs

LITCHFIELD, MINNESOTA 55355 • 612-693-2477

BBC Brown Boveri Turbomachinery, Inc. **1891**
BROWN BOVERI
Established

• Industrial Gas Turbines • Medium & Industrial Steam Turbines • Turbogenerators • Turnkey Power Systems •

711 Anderson Avenue North
St. Cloud, Minnesota 56301
Area Code 612 - 255-5211

ALBERT L. SCHEIDELER
PRESIDENT

September 18, 1981

Mr. Vin Weber
514 Cannon Building
Washington, D.C. 20515

Dear Mr. Weber:

I understand The Small Business Subcommittee on Tax, Access to Equity Capital, and Business Opportunities, will be holding its second hearing on Job Creation and the Revitalization of Small Business on September 22. During that hearing the impact of interest rates on current small business practices will be reviewed. We at Brown Boveri Turbomachinery, Inc. (BBT) believe that high interest rates affect us adversely in at least four areas:

External-Customers

As you may be aware, our gas turbines and steam turbines have selling prices measured in millions of dollars, and one turbine order means additional employment security for citizens of Minnesota. High interest rates make it more difficult for a potential customer to justify the purchase of our products, as they have both a relatively large price and a relatively long depreciable life.

External-Vendors

Our turbines contain parts and components that have high values and long procurement cycles. High interest rates add to our vendors' costs and tend to increase the prices BBT must pay for purchased items, which in turn makes it that much more difficult to sell a turbine.

Internal-Company

In the same way that potential customers have difficulty in justifying purchases of plant and equipment when interest rates are high, so does BBT have difficulty in justifying the purchase of more productive equipment, as well as in stocking inventory to serve customers better. Both aspects work to make BBT less competitive, and especially so in the international arena.

Internal-Employees

BBT employees, as other Americans and in particular the younger members of the work force, have an added problem from high interest rates if they are trying to finance the purchase of a home or an automobile or similar basic needs.

General

Federal efforts to reduce the ravages of inflation certainly require the highest of priorities. Hopefully, some ingenuity can be brought to bear on the collective problems to relieve the difficulties that high interest rates cause to so many people and businesses.

Sincerely,

Al Schindele

ALS/lm

ELK RIVER VETERINARY CLINIC
948 HWY. 10
ELK RIVER, MN. 55330
(612) 441-5111

Dear Mr. Weber,

My profession is Veterinary Medicine and I am a sole proprietor since 1977. Interest rates have risen from 10½% for my original equipment loans to 18½% on a loan that I obtained just 2 months ago. My business is bordered by established Veterinary Hospitals. Although I have purchased most of my equipment at lower interest rates (10½ to 13%), the majority of my capital outlay involves construction of a hospital.

An attempt to construct a hospital at the present rate of 18-20% would make it extremely difficult for me to compete with the existing businesses. I operate my business in a very efficient manner, and feel that I am very competitive; however the established hospitals have the interest edge over me and can and do maintain lower fees because of lower overhead. I don't mind competition on an equal basis, but with the large difference in interest rates in an investment of $250,000 adds a great deal of overhead to an already very competitive price schedule. (The profession was just investigated over a 5 year period by the Federal Government (FTC?) and was found to be price competitive throughout.

I personally feel at an extreme disadvantage under the present interest rates. The current high rates are preventing me from establishing myself in the community with a more suitable facility and preventing me from hiring an additional Veterinarian and lay help; which could be incorporated into a larger facility.

In conclusion the high rate of interest has in effect reduced fair competition in my situation. Thank You.

Sincerely yours,

David A Gilgenbach DVM

David A. Gilgenbach DVM

jr

REDWOOD FALLS SAVINGS AND LOAN ASSOCIATION

Post Office Box 317
WASHINGTON AT THIRD STREET
REDWOOD FALLS, MINNESOTA
56283
Telephone 507 [illegible]

Branch Office
Post Office Box 127
824 E. Lincoln Ave
Olivia, Minnesota 56277
Telephone 612 523 2040

September 18, 1981

Congressman Vin Weber
514 Cannon Office Building
Washington, D.C. 20515

Dear Congressman Weber:

I received your letter of September 14, 1981, concerning the Small Business Subcommittee on Tax, Access to Equity Capital, and Business Opportunities hearing on September 22, 1981, on Job Creation and the Revitalization of Small Business. I wish to thank you for this opportunity to give you my thoughts and also for the comments you made in Redwood Falls, Minnesota, earlier this month.

The impact of continued high interest rates on our economy are devastating. If these high rates continue much longer many marginal small businesses will be out of business. Some of the neighboring towns that we serve have already lost long established car dealers, implement dealers, realtors and many other businesses solely due to high interest rates. They had managed for years and we have a very good well-diversified economy in rich farm country. Our farms are mortgaged to the hilt. We need lending rates in the 12-14% category or lower in order to function.

Redwood Falls Savings & Loan Association has assets of $30 million dollars and has full-time offices in Redwood Falls and Olivia, Minnesota, serving Redwood and Renville Counties since 1924. We are losing money and will pay little or no income taxes this year. Construction of new homes has come to a complete stop and the sale of existing houses are few and far between. Contractors and related industries are out of work.

SAVINGS NOW INSURED TO $100,000.00

The following statistics will point out what we are saying:

Real Estate Loans Originated or Purchased
Redwood & Olivia's Loans As of September 1, 1981

Year	Number of Mortgages	Amount	Average Interest Rate
1976	167	$3,847.155.81	8.75%
1977	187	4,145,139.90	8.75
1978	189	2,708,795.56	9.25
1979	98	1,461,320.00	10.25
1980	46	378,100.00	13.25
1981	9	23,000.00	15.00+

Our Savings & Loan has been profitable and has served this area with most of the home loan money for many years. We now have a negative spread on our mortgage portfolio and are paying the saver high market rates in order to maintain our liquidity. It is at best a short-term arrangement as we patiently wait for the magic of the economic package to work.

If the Administration and the Federal Reserve would let interest rates fall to their natural level, Savings & Loans around this country would become profitable overnight. Above all, this must happen. What are the prospects of it happening on its own? Not very good since the Administration and the Federal Reserve have artificially kept interest rates high as their method of fighting inflation. IT DOES NOT WORK!!! Savings and Loans are the victims of this policy since we cannot raise our rates on our fixed-term mortgages, and our "decontrolled" liabilities have skyrocketed. For small business this is too great a price to pay to beat inflation. The cure is worse than the illness.

I am of the opinion that we are "deregulating" our business and many others too rapidly. This is especially true with volatile interest rates and uncertain times that we are in. We in the Savings & Loan business need: (1) reduction of interest rates by the Federal Reserve, (2) a program by the Federal government to purchase our low yielding loans, and (3) a program of aid to S & Ls rather than simply getting rid of them by forced mergers. The All Saver Certificate should help some but is not the complete answer.

We can house this nation and turn the whole economy around with lower interest rates and a stable set of rules we can bank on. Most American's number one priority is home-ownership and it is so important to maintain this possibility. Many peripheral small businesses and jobs are dependent on our industry for their existence.

Thank you for your consideration.

Sincerely,

REDWOOD FALLS SAVINGS & LOAN ASSOCIATION

Paul W. Pryor

Paul W. Pryor
President

PWP:plh

dci
INC

P.O. BOX 1227 — 600 N. 54th Ave. — St. Cloud, MN 56301 — Tel. 612-252-8200

September 18, 1981

Congressman Vin Weber
514 Cannon Building
Washington, D.C. 20515

Dear Vin:

Thanks for contacting me relative to the impact current interest rates are having upon our business practices.

I recognize that the complex problems of controlling inflation and interest rates, both of which have occurred at the same time, are difficult problems to resolve.

The impact of currect high interest rates is having a disastrous effect upon many small businesses. Fortunately, we have fared better than most due to present product demand and what we feel are tighter than normal internal financial controls. Our local bank has also been willing to give us a break in the interest rate charged on monies lent within their limit but the credit overline money is costing us above prime rates.

I trust that my comments will be of value at the September 22nd hearing.

Sincerely,

Carl
Carl F. Nielsen
President

CFN:db

Enclosure

distinguished Craftsmanship for Industry in stainless steel

dci
INC

P.O. BOX 1227 — 600 N. 54th Ave. — St. Cloud, MN 56301 — Tel. 612-252-8200

September 18, 1981

To: The Small Business Subcommittee on Tax, Access to Equity Capital
and Business Opportunities.

Gentlemen:

As President of DCI, Inc., St. Cloud, Minnesota, Past Chairman of the Minnesota Association of Commerce and Industry, Vice-President of St. Cloud Opportunities, Inc. (a non-profit business development group), President-elect of the Dairy and Food Industries Supply Association, Washington, D.C. and past delegate to the 1980 White House Conference on Small Business, I submit my concerns as to the impact high interest rates is having upon Small Business.

First I'll relate to our own business activity and the effect high interest rates have had upon us.

1. Expansion plans have been laid to rest until interest rates are lowered.
2. Interest costs have given larger corporations a competitive advantage.
3. Our suppliers have reduced inventory levels to an all-time low. This, when we are also trying to reduce inventory, creates untold scheduling and production problems.
4. Purchase of machinery and equipment for improvement of productivity has also been tightly controlled and/or delayed.
5. Customers which are small in size are delaying the purchase of new equipment.
6. Profit is affected which reduces dividend and borrowing capabilities.
7. Large corporations (our customers), in some cases, are imposing tight purchasing controls limiting purchases without total management approval to $500.00. This low limit dictates no purchase of capital equipment such as ours.

Secondly, and speaking for all Small Business, I submit the following information:

1. Job creation in our area has come to a standstill. Home building is at an all time low and when one major large corporation's expansion project is completed, carpenters, masons, electricians and steel workers in the area will join the unemployed.
2. Last week the Board of Directors of St. Cloud Opportunities, Inc. were told that a local large corporation project in our Industrial Park may be postponed indefinitely. Many small businesses would have participated in that project.

3. In contact with small business persons on several occasions, I can say that interest rates are their major concern now - last year it was inflation. Two small business people, one being an enterpreneur who started his business three years ago in an undercapitalized position and built his employment in manufacturing up to sixty-five employees, talked to me last week about his financial situation. My guess is that he will be forced out of business because the equity ratios require much higher than normal above prime interest to the lending institutions. Because of business reverses and high interest rates coupled with a high risk factor a forty-three year old small business in Southwestern Minnesota is headed for bankruptcy.
4. Independent retailers of all types of merchandise; farm machinery and auto dealerships; building and general contractors and small manufacturers are either out of business or on the verge of collapse when profit margins cannot support the cost of money. Some have already failed in our area.

I am an advocate of the Free Enterprise System and the principle of supply and demand. The money demands of government has reduced the money supply and until that demand is reduced interest rates will remain high. Cuts in government spending are encouraging signs and the new taxation and depreciation rates will eventually allow business to accumulate capital resources. Reduction of waste in government and correction of the abuses in many of our social programs would also do much to increase the money supply in the private sector. The concept of Small Business Participating Debentures (SBPD) as recommended by the White House Conference on Small Business as a new form of security could conceivably be a source of lower cost capital for Small Business. Congress should explore that as a means for Small Business assistance and take action necessary to make this legally acceptable.

Sincerely,

Carl F Nielsen

Carl F. Nielsen
President

CFN:db

MORGAN HATCHERY, INC.
Howard W. Voelz, Pres.
Morgan, Minn. 56266
Phone 507-249-3187

Howard W. Voelz
Box 274
Morgan, MN
56266

Honorable Congressman Vin Weber.

I appreciate your writing to me asking my opinion on how the high interest rates are effecting small business and farmers today. Being a small feed store I hear alot of different angles and what impact it has on us.

Small business today cannot expand with this high rate of interest. I know that the economy could not keep going at the rate of inflation that we were having. That would been just as devastating as high interest rates, but I believe that expansion has come to a screeching halt. Today it is near impossible to borrow any money at the high rate and make it come out. The farmers are not borrowing money to pay bills, borrow money at 19% to 16% isn't sound management. Thus business must have to borrow to keep in business.

Expansion is out today. On a $100,000 project I was looking at, my interest would have been 19% or $19,000 a year just for interest, I could not make it come out thus not building. That means staying the same which is not moving with the world. If small business fails so does the competitive society. That hurts everyone

Speaking in behalf the farmer, we have had alot of young farmers go back to the farm in the last 5 to 10 years which is good, but if he cannot compete he is lost by the wayside. High interest is very hard on them, their cost of raising livestock or growing crops has just about doubled with the rate of inflation that we had, now with high interest he is hurting along with the rest of us.

I admit that interest rates just cannot drop to a lower rate over night or we would have a rate of inflation just as high if not higher than before.

Right now all the young business men and young farmers are looking for is a ray of hope that interest rates will come down so that we can stay in business and keep this great country going.

I hope you can read my writing but it is easier for me to write long hand than it is to type.

Thank you again for asking my opinion on what interest rates are doing to the small business man and young farmer. I am very interested and hearing the out come of your hearing.

Thank you again

Sincerely

Howard W. Volz

COMPLETE BUILDING SERVICE

Mille Lacs Lumber and Supply

ONAMIA, MINNESOTA 56359 TELEPHONE 532-3129

Sept. 19, 1981

Honorable Congressman Vin Weber
House of Representatives
Washington, D.C. 20515

Dear Congress Vin Weber:

Thanks for your letter of Sept.14 regarding the impact of interest rates on small businesses. This is something the whole country should be concerned with.

Even with the cutbacks that President Reagen is working on, the plan is to balance the budget by 1984. In other words the government will be having a deficit going in debt farther each year. The Democrats sure left office with a dilly of a deficit spending program. (Trouble is people on welfare federal handouts and receiving food stamps can vote). From this point of view of going farther in debt it looks like Volcker's plan on high interest will continue until the budget gets balanced, hence continued high interest.

At the present time we are paying our local bank 19½% interest on short term notes. We actually are borrowing more from a private party at 15% than we do from the bank. Some small businesses are doing this.

We enclose a statement of our sales for the years 1978 through 1980 with a projected sales figure for the year 1981. You will note the interest we pay in proportion to our sales has gone from 1.7% to 8.5%. Please note how the salaries and wages have gone also.

I must mention that our family owned corporation has now two less full time employees and two less trucks to deliver. We had to pull in our horns in this distressed county due to the terrific drop in our house and utility building construction. Our salary per cent will drop considerable next year since one more will work just part time and draw Social Security.

If our business was in a more congested area we would go cash and carry but hesitate to try it in a small rural community.

Sincerely,

Les C. Sievek

	Sales	Interest paid % of Sales	Sal. & Wages
1978	1,153,000.00	1.7%	7.2%
1979	949,700.00	2.4%	9.2%
1980	755,800.00	3.3%	12.8%
1981	450,000.00Projected	8.5%	13.7%

THE CLARA CITY Herald
CLARA CITY, MINNESOTA 56222
Your Hometown Newspaper Since 1895
FREE PRESS FREE PEOPLE

Friday, September 18

Congressman Weber:

I would like to thank you for the opportunity to express my thoughts and relay my experience with regard to the impact of interest rates on current small business practices.

After receiving your letter I sat down with one of the local bankers to get a little better idea of the effect that current high interest rates are having on small business and farming in our small community as a whole.

Clara City, as you know, is a small community of approximately 1,600 population. We have beautifully rich farm land surrounding us, and we depend to a large extent on the farmers for our welfare. "If the farmers do well, we do well."

The high interest rates have reduced the purchasing power of the farmers to a level that we have scarcely seen before. This, combined with the current low prices for agricultural products, is cause for concern among the retail business people on main street.

It would be safe to say that 50 to 75% of the small business people in this community do not have enough cash to operate their businesses without borrowing money on a regular basis. Consequently, the high interest rates have eliminated some businesses and have curtailed operations among others. The overhead must be cut down so we cut down on the number of employees that we hire, causing more people to file for unemployment benefits. New business start-up is virtually non-existant or very difficult at best.

Ever increasing employer contributions to the Social Security system and continuously increased minimum wage rates discourage expansion and productivity. As you know, Vin, I have the local weekly newspaper in Clara City. We have an annual gross of less than $100,000. My father and my uncle were partners in this business since 1936, and they managed to make a living. After going away to college I returned in 1966 and took over the business in 1970. I am 41 years old; I have a son who is 13. If he were interested in being the third generation of Swansons to run this business, and if I thought he could make a respectable living at it, I would be proud to have him carry on. I not only doubt whether he will have the opportunity to succeed me, I doubt whether I will be able to retire from this business myself. The future is that uncertain.

I do not see a future in small business if existing economic conditions persist, and this is indeed unfortunate, because the farmers and small business people living and carrying on commerce in towns of 1,600 people are and have been the backbone of this nation.

Thank you for taking the time and concern to approach me on this matter.

Sincerely yours,

Kermit Swanson

Kermit Swanson, Editor

Coca-Cola Bottling Company, Inc.
of Marshall, Minnesota
407 East Main Street/Marshall, Minnesota 56258

September 18, 1981

Senator Vin Weber
514 Cannon Building
Washington, D.C. 20515

Dear Senator Weber:

I appreciate your giving me the opportunity to give my opinion on the affect of high interest rates on small businesses such as mine.

I'm sure it has all been said before, however; we must continue to remind those in a position to do something about it, just what high rates are doing to the progression and productivity of business in this country.

I am a member of the board of directors of a local bank. I am seeing first hand what the high cost of money is doing to our local farmers and businessmen that must borrow money to put their crop in the ground or support their accounts receivable.

In our area the price of farm land has been appreciating steadily for several years as it has all over. This obviously has improved the net worth of our farmer and has increased his borrowing power. This is good and bad. This has provided him a way to get increased cash to meet rising operating costs. He has no choice but to borrow this expensive money if he is going to continue farming.

Banking ag people estimate we will lose 30% of our farmers if land ceases to appreciate. Local banks already are staring to cash in some farmers.

Interest rates obviously are not the only contributing factor to the farm problem, but they certainly are a major factor.

As for myself, we are simply in a holding pattern. If we don't have the money in our fist we don't buy. There are several things I would like to do to improve our efficiencies and possibly expand, but there is no way I can achieve a return on borrowed money to pay back a 20% interest loan.

As you may be aware, the soft drink business is highly competitive at both national and local levels. Operating efficiencies are extremely important in the survival of the small bottler as myself. We must be in a position to provide our products in the types of containers our consumers want. If we cannot afford to buy the necessary equipment to produce and distribute these packages then we are not competitive and our demise is eminent.

There used to be 1,100 franchised Coca-Cola bottlers in the U.S. There are now less than 500 serving the same geographical area. This trend is also typical of other franchised brands.

Up until a few years ago we competed with other soft drink companys that were similar in size. Today, some of these have sold out to large multi-franchise operations and we find ourselves competing on the same battlefield, only some of the conditions and rules are changed. Our new competitor has vast resources to draw from and we must be better than ever if we are going to survive.

We must become more profitable, so we have more dollars to reinvest in our business in order to maintain efficiencies and offer products the consumer wants. If we cannot do this and have to borrow 20% money, the end is near. The soft drink business does not traditionally yield the kind of profits necessary to pay back high interest loans. Certainly many other businesses are in the same boat.

We have our belt cinched up tight now and have one or two notches left. Those that don't have a notch left are in big trouble unless there is some relief from high interest money.

Sincerely yours,

COCA-COLA BOTTLING CO., INC.

John Sherman

John Sherman

JS:sh

Edgerton Rendering Works
H. L. KOOIMAN and PAUL C. WARD
P. O. BOX 367
EDGERTON, MINN. 56128
PHONE: (507) 442-6211

September 18, 1981

Hon. Vin Weber
Congress of the U.S.
House of Representatives
514 Cannon Building
Washington, D.C. 20515

Dear Vin:

In response to your letter of September 14, 1981 pertaining to the impact of high interest rates on current small business practices, I submit the opinion of my partner and I.

Because of the high interest rates the farmers can not afford to have many animals other than the absolutely necessary ones to barely exist. With fewer animals on the farm then the fewer will die and therefore we get fewer in and likewise, less income.

With high interest rates people can not afford to eat as much meat so the butcher shops have less work and with that less trimmings which is another product that we process.

With less product to process, naturally, we have less finished product and need less help.

Just prior to the increase in the interest rates we expanded our facilities at a cost of $130,000. which for a business our size is a large amount of money. Since then we have been forced to borrow an additional $50,000. just to stay in business.

My partner and I used to make approximately $25,000. per year profit. Last year we made $4,900. and this year it looks worse so far.

The bank has informed us that we must get some of this paid off or they won't be able to finance us any longer. So, if things don't change pretty soon we will be out of business. This business was started in 1924 so it isn't just a new business.

We can't just charge more for our finished product like many businesses. Our product is sold on the same basis as the farmers product, according to the market rather than according to costs.

Interest rates are a major factor with our problems but they aren't the only problem. Insurance rates such as workmen's compensation, liability and other insurances are another cost that is eating us up. Besides that the payroll taxes are taking a bigger bite out of our income each year also.

I feel the answer is not in cutting the income taxes but in cutting the national debt. In the long run we as a nation would be much farther ahead. Just as my business would do much better to pay off debt rather than continually borrow more and pauing high interest in addition. This also would increase the amount of available money and therefore bring the interest rates down.

Another thought I have concerns Social Security. There should be a law that a person may not draw out more than they contributed except for disability. No other insurance would allow you to pay a minimum amount and draw for the rest of your life like social security has. It is poor business sense.

I know of several persons that paid minimum quarters and drew for many years until the man died and after that his wife drew for many years. In one particular case, they are quite wealthy and it is just increasing their estate which is quite sizeable anyway and it is at the expense of social security.

If they can't get along on what they receive they should be getting welfare for the rest. Social Security shoudl not be a welfare program whether the person is rich or poor.

In general I think President Reagan's policy is very good but I feel that that there are still many, many places that the federal spending can be cut. The federal give away programs for smaller units of government is a good example for the costs of these projects soar when the federal government is involved.

Sincerely,

Paul C Ward

PAUL C. WARD

Telephone 295-2711
Metro Line 333-5739

City of Monticello
250 East Broadway
MONTICELLO, MN 55362

September 18, 1981

Representative Vin Weber
514 Cannon Building
Washington, D. C. 20515

Dear Representative Weber:

In a separate letter I have addressed the impact of interest rates on my mortuary business. As mayor of Monticello, I would also like to share with you how the present interest rate and status of the economy affects our citizens in the community here.

Approximately one year ago, several doctors announced their intention of setting up a specialty medical clinic in Monticello. This announcement was warmly received by the community since this clinic would offer medical services which formerly were only available in St. Cloud or the metropolitan area of Minneapolis and St. Paul. At this point in time this project is all ready to go with one exception: the high rate of interest. Obviously, there is a concern among the citizens that if economic conditions do not improve, Monticello will lose this opportunity for such medical services.

In addition to the medical clinic, there have been three other projects that have come before the council, been approved and have been unable to start because of the high interest rate. These three projects involve small businesses, including a budget motel, a professional office building and an office-warehouse complex. The office-warehouse complex would have been a great asset to the community of Monticello since it would be a speculative building that could be leased by industries wishing to relocate to our city.

One other item that I might mention, is that on September 14, 1981, the city of Monticello sold $490,000 of General Obligation Improvement Bonds at an interest rate of 11.61%. This is 3½% more than the previous issue the city of Monticello had on January 12, 1981. This interest cost will be borne by the residents and other small businesses that benefit from the improvement.

Welcome to Monticello . . . little mountain

Representative Vin Weber
Washington, D. C.
Page #2

Obviously, businesses both large and small are being affected by the high interest rates. However, it is particularly drastic for the small businessman who does not have the capabilities of internally financing his business or has no varied or alternative lines of credit established that a larger business might have.

Thank you again, for the opportunity to submit input on this very important issue.

Sincerely,

Arve A. Grimsmo
Mayor
City of Monticello

AAG/lsg

KQAD AM & FM Stereo
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FM 100.9
Phone 507 283-4444
News, Weather, Sports, Farm Markets
Box H • Luverne, Minn. 56156

Sept. 18, 1981

Rep. Vin Weber,
House of Representatives,
Washington, D. C. 20515

Dear Mr. Weber:

In response to your letter regarding the biggest problem facing small business today, it is without question, high interest rates.

I talk with different businessmen throughout three counties about every week. Many are really hurting financially. People charge to them and they have to borrow from the bank to keep in business and the high interest eats up the profit. It's easy to say that they should charge the customer, but it is very hard to do in a small community where someone has been a life-long customer.

Then there are the car dealers, implement dealers and those with high price items for sale. People will not buy and pay the very high interest rate. These businesses are in real trouble.

Small business cannot expand or remodel if they have to borrow money. We have a company at Luverne who had over 300 employees. They have now gone under and now those employees are without work. I cannot blame the entire downfall of the business to high interest rates, but it sure was one of the factors. They had to borrow over $2,000,000 and were paying top interest rates.

If these interest rates remain, thousands of small businesses will close and soon a few big businesses will own and operate everything as if in a monopoly.

Another problem is your banks and savings and loan associations. They must pay the high interest rates on savings and then cannot get people to borrow the money at a higher rate, so they are losing money. I think you have heard of many savings and loans closing.

Congress raised the retirement age, which certainly did not help our unemployment problem. In this area it really won't make any difference

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-2-

as most businessmen are so sick of government regulations and interference that they, or a majority, want to retire as soon as possible.

High interest rates, high taxes and a government that continually wnats to take what is ours, has hurt productivity as a nation, because people do not enjoy working anymore.

Another thing that does not have to do with high interest rates, but is a big concern and that is Congress wanting to cut Social Security Benefits. This is not your money. It is ours. We have been paying in since 1936. Because Congress takes out millions of dollars for things other than Social Security, the fund is in trouble. Who's fault is this? Not the employer or employee who have contributed every single year. It's Congress and they must shoulder the blame.

Yours truly,

Harold L Norman
Harold L. Norman

P. S. These remarks are my own personal opinions and not necessarily those of the radio station.

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Col. DON FITZNER
AUCTIONEER

Phone: (612) 523-1392 or 523-1889
1610 West Lincoln — OLIVIA, MINN. 56277

September 18, 1981

Vin Weber
514 Cannon Building
Washington, D.C. 20515

Re: Committee on Small Business

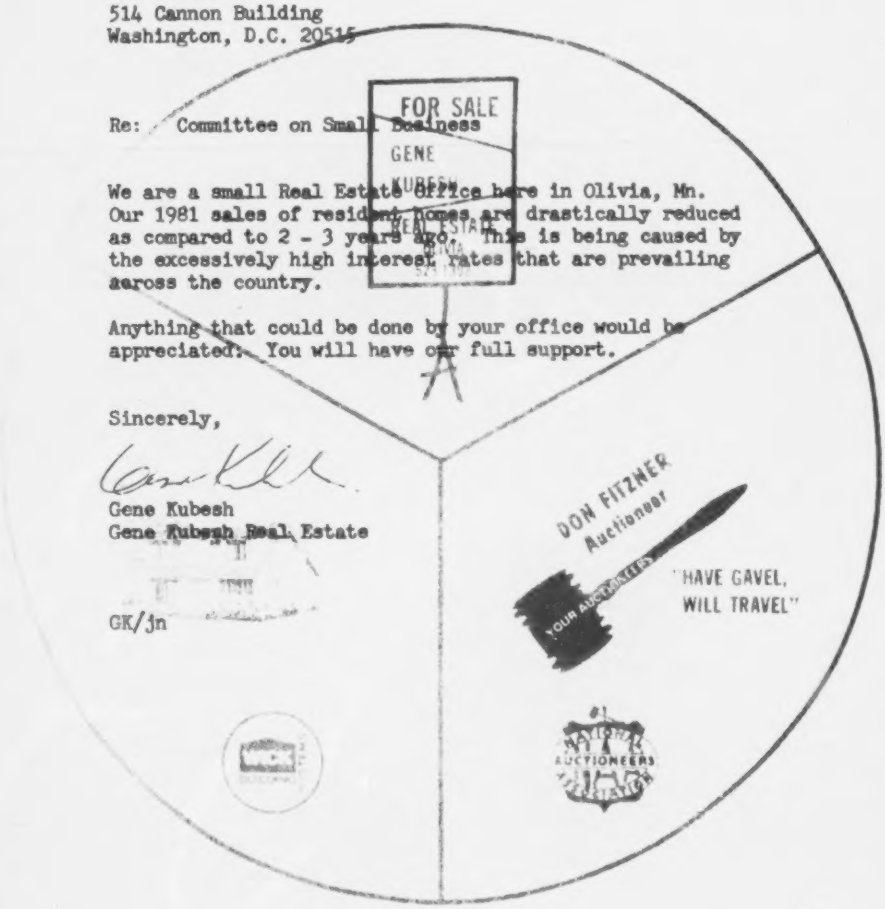
We are a small Real Estate Office here in Olivia, Mn. Our 1981 sales of resident homes are drastically reduced as compared to 2 - 3 years ago. This is being caused by the excessively high interest rates that are prevailing across the country.

Anything that could be done by your office would be appreciated. You will have our full support.

Sincerely,

Gene Kubesh
Gene Kubesh Real Estate

GK/jn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WICK

GLUTH OIL COMPANY
Box 387
Morgan, Minnesota 56266
phone: 507 249-3161
249-3195

Sept. 18, 1981

Vin Weber
Member of Congress

Dear Congressman:

I am writing in regards to your letter dated Sept. 14, 1981 about the impact of interest rates on small business's. I have gone over my profit and loss sheets which I get from my accountant, there is quite a difference in the amount of interest I have paid for the same period of time in 1980. I have two small Oil Companies which I operate seperately, Clements Oil Co. at Clements MN. and Gluth Oil Co. at Morgan, MN. At Clements the interest has almost doubled in the 184 days of business this year. My accounts receivables are a little higher then the same period a year ago. In 1980 March 1 to August 31, 184 days was $4,447.41 which is 10.2% of my expenses. In March 1 to August 31, 1981 my interest paid was $8,040.95 which is 18.2% of my expenses. Gluth Oil Co. at Morgan has also taken a jump, April 1 to August 31, 1980, 154 days interest paid was $12,303.49 which is 19.2% of my expenses. April 1 to August 31, 1981 I have paid $20,465.95 which is 34.9% of my expenses, my accounts receivables at Gluth Oil are down $10,000.00 from this same period a year ago.

As you can see the interest rate is really hurting both company's. It's at the point that I will possibly have to lay off one person from each company. At Clements Oil I employ three (3) full time people and one (1) part time bookkeeper. Clements Oil is a Service Station and Bulk Petroluem. Gluth Oil is strictly Bulk Petroleum, we have one (1) employee besides my wife and I.

With the interest the way it is right now I am very seriously thinking of letting my employee at Morgan go and one at Clements also.

I don't know what the solution is for bringing down the interest rates but it sure is hurting a lot of business's and farmers. I hope something can be done soon or I'm afraid a lot of people which have to borrow money cannot survive.

Yours truly,

Denis W Gluth

Denis W. Gluth

P.S. I think you are doing a good job Vin, keep it up!

PHONE: 329-8354

FULLERS INC.
RENVILLE, MINNESOTA 56284
McCORMICK TRACTORS and MACHINES

SYMBOL
OF
SERVICE

September 18, 1981

Vin Weber
Member of Congress
Washington, D.C.

Dear Sir:

The current situation in regard to unreasonably high interest rates is disasterous. We have a retail store, employing 12 people and sales of $3,000,000.00 If this continues our sales may become $2,000,000.00 and employment 1/3 less. Taxes paid to state and federal government will amount to nothing. We will be asking for refunds under income averaging.

We are placing orders for next year for about 50% of this year. We cannot afford to stock a million dollars of machinery at 20%. This means that our suppliers will be laying off workers who won't be paying taxes, but rather drawing unemployment compensation.

Our farmers in this area are also suffering from very low commodity prices. There will be a larger number than usual of farm auctions this winter and next spring. Another six months of present conditions will see a number of our type of businesses decide it isn't worth the struggle against these problems.

I'm sure my statements would be supported by all farm implement dealers in our area.

Yours truly,

Fullers Inc.

THE COUNTRY TRAVEL STORE
GEORGE E. JOHNSON * Prop
295-3350 / Mpls./St. Paul Toll Free Number: 338-1667

September 18, 1981

Congressman Vin Weber
House of Representatives
Washington, D.C. 20515

Re: Small Business

Dear Vin,

The greatest problem I have today as a small business is the availability of capital at a reasonable interest rate.

In my business, I am compelled to make deposits to hotels, tour operators, airlines etc. to hold reservations for my clients. In the cases of large group tours, this advance money can become sizeable. There is no way I can remain competitive to the larger conglomerates.

This advance money for the most part, is sometimes up to a year in advance. In many cases I simply have to remove myself from attempting to compete.

Sincerely,

George
George E. Johnson
THE COUNTRY TRAVEL STORE

GEJ/mj

124 W. BROADWAY / MONTICELLO, MINN. U.S.A. 55362
AMERICAN SOCIETY OF TRAVEL AGENTS
ASTA

Lamberton, MN 56152
September 18, 1981

The Honorable Vin Weber
Small Businesses Sub Committee
514 Cannon Building
Washington, D. C. 20515

To the members of the committee:

It was our opinion (mine particularily) that inflation was our #1 problem at the beginning of 1981. This seems to be easing somewhat to the point where, presently, interest rates have taken over as the #1 problem on the list.

Example: As a retailer working on a margin of 25-30% with 2-to-3 turns per year, the percentage cost of interest on money needed to operate makes it impossible to expand either inventory, remodel, or improve present facilities or services. We must maintain a status quo or try to pay present bills without anymore borrowing at 17% to 20% interest.

This, then, puts each business person in a vulnerable position to either going out of business while still solvent or wait for bankruptcy. Many retail businesses are either closing doors completely, or cutting their inventory and services in order to survive, hoping the economy will turn around and interest rates will come down.

Because of the 18% interest rates the farmer can not or will not invest in any major purchase. This then starts the snow ball effect. The business man, his employees, the community, the state (sales tax as one example) and eventually the federal level all feel the pinch.

The largest culprit in this whole mess is the borrowing by the Federal Government. Anyone with money to invest will surely put it in Government Bonds or notes at the highest guaranteed rate of interest. This then takes away local monies from not only the banks but also keeps them from investing in any purchases.

Another problem: If I were trying to find a buyer for my business, or my farm, why would the prospective buyer invest in something with possibly a return of zero to probably 2% net when he is guaranteed from the Federal Government 18%? We are a community of 1000 population and need a restaurant BADLY! It has been impossible to find anyone willing to invest or borrow at this amount to finance such a business.

I hope that this supplies you with the information desired. Thank you for your interest in our plight.

Sincerely yours,
Robert Krinke
Our Own Hardware & V Store
221 S. Main
Lamberton, MN 56152

KLASSE Sales and Service

WESTBROOK, MINNESOTA
Ph. 274-6166

9-18-81

Dear Mr. Weber

Per your 9-14-81 letter, high interest rates are not only killing small business, but its also going to get the big ones too! Im surprised the people running our country haven't figured this out yet! Aren't you? Keep it up and you'll force me to retire early yet.

Sincerely
Jim Klasse

KLASSE SALES & SERVICE
Westbrook, Minn. 56183

Village Tool & Machine Co.
133 SOUTHWEST COUNTY ROAD 18 • OSSEO, MINNESOTA 55369

September 18, 1981

Dear Congressman Weber;

Ican give you my experience on interest rates and business activity in one sentence.

As the rates rise, business for me slows ontill at about 20% it stops nearly completely.

Sincerely,

Ted Lindstrom

abs
data
systems
corporation
549 25th AVENUE NORTH
ST. CLOUD, MINNESOTA 56301
(612) 253-8734

Dear Congressman,

In the past few months, the high interest rates and their effects have taken their toll on the business that we have in St. Cloud. We've had to reduce wages of some and lay off others. We've seen one of our best customers go broke. We must be able to get our money cheaper and keep our prices stable. I don't believe credit or wage and price controls are the answer. The only thing that will work for the long term is if banks believe inflation is coming down and will stay there and consumers must share that belief. I don't think this will happen by budget cutting alone. Some symbolism is necessary. We work more and get paid less but the folks in Washington get a raise. If everyone in government took a 5% pay cut it might be believable. I realize that is unlikely and perhaps unduly hard on folks that haven't had many raises anyway. But, something must be done. Most people I know, believe that when the pressure gets severe, the printing presses will be cranked up again and the situation gets even worse than it was before. I'm sure you have witnessed the cynicism on your return visits to this area. I do hope the President's program works, but I doubt it is enough. We really need some innovative leadership willing to take risks, personal risks, to get this country on the right track.

Sincerely
Wayne Victor

MOORHOUSE TURKEY HATCHERY INC.
U.S. Approved U.S. Pullorum-Typhoid Clean
JOHN H. MOORHOUSE
~~TELEPHONE 612-743-2282~~
OUR NEW NUMBER 612-743-2281
CLEAR LAKE, MINNESOTA 55319

September 16, 1981

Honorable Vin Weber
514 Cannon Building
Washington, D. C. 20515

Dear Vin:

High interest is probably the number one culprit in our business today.

When paying 8-9% interest we had about a 10% profit, but now with 20-22% interest you can see what it has done to profits. We are lucky to break even, and nothing on your equity return.

Sincerely,

John

John H. Moorhouse

HOME OF WROLSTAD WHITE POULTS, EGGS, SMOKED AND OVEN-READY TURKEYS

September 18, 1981

Vin Weber
House of Representatives
Washington, D.C.

Dear Mr. Weber:

In reply to your letter of 9/14/81 addressed to my father, Erik A. Tou, I am pleased to have the opportunity to submit a statement for inclusion in the hearing record of the Small Business Subcommittee on Tax, Access to Equity Capital, and Business Opportunities.

Our family is presently in the process of trying to expand our business, and the current high interest rates are definitely a blockade. The state highway has bypassed Princeton, and we realize that in the future this will affect our business volume.

We now have two small restaurants -- the K-Bob Cafe which seats 78, and the Riverside Deli with a seating capacity of 46 plus a garden court.

The new plan calls for the purchase of two acres of land on the highway interchange for a new restaurant with a seating capacity of about 130 and adequate space for parking.

We have been considering this plan for more than a year, and the financing of the project is our No. 1 obstacle.

At present there are no plans for closing our downtown restaurants. We feel there will be a need for them to serve the business community and the senior citizens who live near the downtown area.

If we are able to proceed with the new restaurant on the bypass, it will create approximately 50 new jobs in Princeton.

Thank you for your consideration in alerting us to your committee hearing.

Sincerely,

Stephen J. Tou

Stephen J. Tou Mgr.
K-Bob Cafe / Riverside Deli
109 So. 5th Ave.
Princeton, MN 55371

CR

Cy Reinert Construction Company

No. Hwy. 10, P.O. Box 46, Phone (612) 252-4993
Sauk Rapids, Minnesota 56379

September 18, 1981

The Honorable Vin Weber
Congress of the United States
House of Representatives
Washington, D.C. 20515

Dear Honorable Vin Weber:

I appreciate your interest in my opinions as to what interest rates are doing to small business. I have enough things I could say to make up more than five pages but in the shortage of time I think I can relay the problems with the present day's interest in a much shorter form.

As a developer of single family homes, multi-family homes as well as commercial construction and development of land but for the most part in the building construction business, we will work with profits of about four to six percent.

When for every dollar we have to borrow at 20% and 21% and sometimes even paying one and two points over and above this rate; we have to turn 3 to 4 times the dollars worth of construction for every dollar we borrow just to break even. And when the building business is as slow as it has been for the past year, we are having difficult times even showing margins of four percent.

I am selling off properties which I have had as income properties to raise more capital for our company because the properties which I am selling do not return me a 20% or 21% return. We are forced to disband areas of our organization which are marginal for profit. This in turn puts more people on unemployment.

Our major efforts are made now just to remain in business with hopes that things will improve and take on a more profitable status. If the present situation should continue for another year without any turn around, most all small builders will be out of business as well as a great number of the larger builders. And this is not healthy for the building industry because we all know lack or loss of competition only adds to inflation which is the very problem we are trying to solve.

Sincerely,

Cyril Reinert

Cyril Reinert

js

LIGHT INDUSTRIAL - - COMMERCIAL - - PRE-ENGINEERED STEEL BUILDINGS - - COMMERCIAL REMODEL

Varpness Implement, Inc.

210 Hwy. 6 S. W.
Renville, Minnesota 56284
Telephone (612) 329-3656

September 18, 1981

Mr. Vin Weber
Congress of the United States
House of Representatives
Washington, D. C. 20515

Regarding: Impact of High Interest Rates on Small Business

Dear Sir

I have a John Deere Farm Machinery Contract which I have enjoyed for the last 30 years, starting as a young man with my three brothers in Echo, Lamberton, and in 1962 at Renville, Minnesota. We had a separate contract for each dealership in each town.

In 1954, most implement dealers were in trouble and not able to move their inventory or meet their current bills. At that time, due to the low cost of money, John Deere Company gave extended terms to the worthy dealers and charged interest for the extended period. As the price of the equipment was not so high, the dealers could discount the equipment and get out from under the interest bearing notes. Today, we have the same situation, only with much different circumstances. The machinery is not selling, combines and tractors are not moving, (this is where the dealer makes his profit), only the low cost equipment is moving. You cannot discount enough to make the large equipment sell. We have equipment on our lot that we had to pay for in May and again in September. On this equipment, we have had to borrow money and are paying 20.5% interest. Our discount from retail price is 23%. To this we have to add the cost of freight, which runs about

Varpness Implement, Inc.
210 Hwy. 6 S. W.
Renville, Minnesota 56284
Telephone (612) 329-3655

2%, so if we have to keep this up for a year, what is going to happen?

This week, my John Deere territory man (Blockman) said he had five old time dealers that were in trouble and they probably would have to close down the dealership due to the high cost of money. John Deere is not giving any extended terms. The Butler Grain Bin Dealer is next door to me. He says he will no longer be carrying any inventory. He will have to sell from a picture.

I understand that for every dollar I retail, that dollar extends out to 42 different people.

In the last 10 years, most implement dealers have been forced to put up new facilities to accomodate the new larger equipment. (4 wheel drive tractors, large field cultivators, and combines with 20' platforms). They are carrying a large load on the cost of the building, which I am sure is not paid in full to this date. In my own case, I do not feel unless there is a sign that the cost of money is going to come down, I will be able to continue. I do not believe you can continue very long losing money. The banks in the community are not that large in size, therefore the loan limit usually stops at about $120,000.

In the rural area, we have just started to get the young people involved in business and farming. Most are heavily borrowed, so that the cost of 20-22% interest has taken the profit away and does not leave much with which to carry on. They are not able to pay on the principal or purchase any new equipment or other necessities.

Varpness Implement, Inc.

210 Hwy. 6 S. W.
Renville, Minnesota 56284
Telephone (612) 329-3655

I also feel that what comes from the land is the basis that our whole economy for the United States comes from. (Crops, ore, oil, etc.). Everything starts here, and if this stops, where will the economy be? If we continue to pay 20-22% interest, I will not have to pay any income tax.

Sincerely,

Wilbert B Varpness

Wilbert B. Varpness

WBV/ca

Dear Congressman [redacted],

I realize t hat a number of small businessmen are having trouble with the high interest rates and it is difficult to obtain capitol for expansion or even f or maintaining inventory in certain cases. I feel however that t he president is on the right course and the only thing right now that can cut interest rates is for the Fed. to expand our money supply further and that would bring on more inflation which would be d isasterous.All of the people in this fair land suffer with inf lation and far fewer suffer from high interest rates,besides the whole glory of this country is that we are given the freedom and the oppurtunity to either fail or to go broke and it is basically up to us as individuals whether we do one or the other. Surely high interest rates are hurting some but the alternative is much worse. for t oo long, too many h ave been dependent on the Govt. to bale them out when t hey got in a financial jame, Government neither has that responsibility nor that right;all govt. must do is for them the oppurtunity to succeed or f ail.

D o not change course and do not print more money-hang tough on the path you have chosen-give it a chance and by the third quarter of 1982 things will square themselves away. The worst thing that could happen right now would be for the Reagan Administration and its supporters to get panicky.

We are on the right track=let's stay on it and with God,s help we will make it into a much brighter future economically than most people can even imag ine. I have no doubt that interest rates will hit 22 to 24 before its any better but better it will g et-just warn the public ahead of t ime that t his is going to happen but it will square itself away if the government just stays out of t he damn thing.

Sincerely,
Chet Anderson MD
C.A.Anderson M.D.

Vin – Personally I think you are voting your conscience and I am sure it is quite close to mine so don't let pressure groups push you away from your sound economic thinking. Really nothing but time can square this away and the free market needs time to adjust. Give it that time.

Am supporting you all the way!
Chet

WRIGHT
ELECTRIC
INC.

Route 1, Box 308 • Buffalo, Minnesota 55313 • 1-682-1059

Vin.

Please Excuse The Hand Written Reply. I Feel The Issue Is Important + my Comment's may be of Some Help.

① Lack of Ready Access To Short Term operating Capital, Results In less Employment + Expansion.

② many Project's we Have Bid on In The Last 18 months Have Been Tabled Due To High Interst. The owner's Are Waiting For A Decreace or. A Trend of Stability. No One Can Project Their Bussiness For Any langht of Time. The Uncertain Condition's of The Financial market stall any Progress In Construction.

③ High Interst Rates Have The Fed + State Governments In Direct Competition with Small Bussiness's, By Having To Burrow For Their Short Fall's. A Lender would much Rather Burrow To The Government Than To Speculate on Small Buss. Thus The Tax Payer's End up Funding Small Buss. Competition. The Short Fall In Buss Revenues Also Add To The State + Fed Problems making A Snowball Effect of The Whole Situation.

The only way I Can See A Clear Route To Easing or Solving This Problem Is To Eliminate Unessary Spending,,

WRIGHT
ELECTRIC
INC.

Route 1, Box 308 • Buffalo, Minnesota 55313 • 1-682-1059

WASTEFULL PROGRAMS, CUT BACK ON BURRCRACY, THIS I FEEL WILL GIVE THE INDIVIDUALS MORE INCENTITIVE TO CREATE + WORK. IT HAS BEEN SAID THAT NO ONE SPEND'S MONEY MORE CAREFULLY THAN THE PERSON WHO EARNED IT

④ I BELIEVE ONE PLUS EFFECT THE HIGH INTEREST HAS IS THAT IT BRINGS ALL OF US BACK INTO PRESPECTIVE WITH REALITY + IN A SENSE FORCES US TO RE EVALUATE OUR BUSSINESS'S + FINE TUNE THEM

THANK YOU FOR THE OPPERTUNITY TO VOICE MY OPINIONS KEEP UP THE GOOD WORK.

SINCERLY YOUR'S

TERRY KORTHOF

Goco Fuel and Hardware
Box 177
Clear Lake, Minn 55319
Sept. 19, 1981

Congressman Vin Weber
6th District, Minnesota
514 Cannon Building
Washington, D.C. 20515

Dear Mr. Weber

It is fortunate that I have the opportunity to express my feelings and financial experience that I have had with my fuel and hardware business during the past nine years.

Many changes have taken place during nine years of business. I purchased the on going business by securing an S.B.A. loan through the cooperation of the local bank at eight percent interest which now is considered very reasonable. It was my disadvantage to find out when securing the loan that it was a loan to be repaid in seven to ten years. That was load enough but there was a limit amount set of how much I could borrow so later I had to borrow more from the bank to complete setting up the store with retail hardware and to have some operating capital. So the load increased but it still would have been OK but the price of fuel and hardware at the wholesale level began to increase at an alarming rate For example, five hundred gallons of Deisel fuel and five hundred gallons of gasoline retailed to the farmer or contractor in 1972 cost $240.00, today the same products retail for $1140.00 The farmer and contractor generally expect at least thirty to sixty day credit and some pay in ninety days. Also there are a few farmers that say they cant pay from the time the crop is planted in May until it is harvested in November.

The point is that the inflationary increase of the products sold is placing a bind on my operating capital so that I am forced to borrow money to survive which makes growth and progress impossible at an eighteen percent interest rate.

When I started the business I felt fortunate to acquire the S.B.A loan, but I asked myself at that time, why can the average American citizen be able to acquire a twenty to thirty year home loan and I can't get a similar loan for the sake of the community, my family and myself to purchase a local business which is a benefit also to the farming community.

When an individual purchases a home loan to repay in twenty or thirty years the amount and interest is set for that period of time, but in a business you are caught with the changing times, with the risks involved, higher prices resulting in increased credit, increased labor costs, higher machinery costs, higher insurance rates, etc.

A possible solution to my problem and a way out of this dilema is some tax relief and a opportunity to refinance the whole business operation at a realistic interest rate along with a sensible amount of time to repay the loan such as twenty or 30 years.

the tax reduction proposals now facing Congress certainly will help and I compliment you and the tax Committee for their effort to help small business, but along with that please investigate the SBA loan situation and interest rates so that a good long range feasible program can be a benefit for people desiring a profitable future in business in the small farming Communities of America.

I enjoy operating a business and my family is working along with me. My nineteen and twenty year old sons are hoping to take over the business and therefore we would like to grow but under the present conditions we are beginning to ask ourselves is it really worth the effort.

Thank you again Mr Weber for taking an interest in this situation and allowing me to tell it like it is.

Sincerely,
Les Goenner

Anderson Funeral Home
THIRD STREET & WASHINGTON AVE. - P. O. BOX 512 - MONTEVIDEO, MN. 56265
ARNOLD C. ANDERSON KENNETH W. ANDERSON

19 September 1981

Honorarble Congressman Vin Weber
514 Cannon Builidng
Washington DC 20515

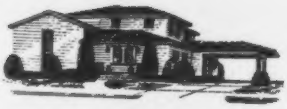
RE: Interest rates, small business, job creation and revitalization of small business.

Dear Honorable Wber;

I am a delegate to the Minnesota Conference on Small Business, which is semilar to the White House Conference on Small business, and I have the oportunity to listen to other delegates who represent small business, farm service business and farmers too. These delegates are from every section of Minnesota and represent every type of small business venture. Suprizingly our problems are the same whether we be large of small or what area of the state we come from.
The cost of doing business (CDB) has risen even faster than inflation and has destroyed and realistic "return on investment" (ROI)for owners or investers. Working capitol is very low and the bank loan rates are too high and riseing and bankers are refusáng loans on marginal profit projections.
You want to know the problems small business is suffering from ?
Government: Federal, State and Local regulations, fees, and add on salary expences (So called workers benifits,to collection amd bookeeping expences.) We have been nickeld and dized to the tune of thousands of dollars for being in business. Government loves those "hidden taxes" that the consumers ultimatly pay by loading up products from raw material, prcessed,manufactured,transported,stored,wholesaled and finally retailed. No wonder a loaf of bread with 6¢ of grain can cost 85¢ to $1.00 to a consumer, there is 70¢ of taxes on it for such things as license fees,real estate taxes, unemployment & compenstion taxes,social security taxes,transportation taxes, taxes on utilities (light,heat,telelphone) and clerical pay for forms and reports & payroll at EACH LEVEL of the food chain. With all the mandated (governement) costs we add the highest interest costs for borrowedmoney. The Federal Reserve Board raises interest and tightens money supplies to cure inflation, but their cure is killing the pateint (small business) and not curing inflation.
It's paradoxical that the Federal Reserve Board, which is not a government agency controls the money supply and sets interest rates and is all powerfull and answers to no authority !
The only group to make a profit & prosper today is the large banks who have made the highest profits during our recent inflation,deflation,recession or and other fiscal cycle. I give them credit for intelegence,delegence and oportunism, but the coincedence of their sucess can only be explained by

~~page 2~~

Anderson Funeral Home
THIRD STREET & WASHINGTON AVE. • P. O. BOX 512 • MONTEVIDEO, MN. 56265
ARNOLD C. ANDERSON
KENNETH W. ANDERSON



Honorable Senetor Vin Weber

RE: Interest rates, small business, job creation and revitalization.

the bankers moves prior to any Fedral Reserve Board's actions. There was a great deal of indignationm to the oils company profits these last few years but that's peanuts compared to the banks profits now, and these profits are coming out of small business. Our profit margin has steadily declined and the interest rates have wiped it all out and is wipeingout many small businesses today.
What small business can afford to create new jobs today? who can afford to pay the heavy job payroll taxes? who can afford such unreasonable high interest rates ? small business can"t ! (only bankers)

Respectfully,

Kenneth W. Anderson

Kenneth W,Anderson

H. Ruppert & Son Well Co.
20420 CO. RD. #50 · HAMEL, MN 55340 · PHONE 425-3202

9-19-81

Hon. Vin Weber
House of Representatives,
514 Cannon Building
Washington, D.C.
20515

Dear Mr. Weber:

Thank you for mentioning hearings of the Small Business Subcommittee on Tax, Access to Equity Capital, and Business Opportunities.

As mine mentioned to you before, probably the biggest problem facing small business today is high interest rates. In our case we get the results of this policy from both sides. One, we must pay high interest rates on money we borrow to finance equipment purchases, inventory, etc.

Secondly since we drill water wells and install septic systems, a large proportion of our work is on new construction.

High interest adds tremendously to the already high cost of housing and small commercial construction.

We think the statistics as reported in the past weeks Mpls. Tribune are only now starting to catch up with reality (single family housing starts lowest since 1939, etc)

H. Ruppert & Son Well Co.
20420 CO. RD. #50 · HAMEL, MN 55340 · PHONE 425-3202

②

9-17-81

Hon. Vin Weber

From our viewpoint, single family construction is at a virtual standstill. We have many customers, small builders who have built one, two, or maybe no houses this year, as against the six, twelve or eighteen they would normally construct.

What about the potential buyers of these houses? For many, the dream of home ownership will remain unfulfilled only because of artificial barriers or hindrances, such as high interest, govt. regulations on various levels such as selective areas only for F.H.A. & V.A insured mortgages, zoning, rules on type & size of dwelling, amenities such as garages, paved drives, size of lots now mandatory in many places, & many other rules that serve to raise the price beyond those of us of average means.

Added to this, of course we have all the other government regulations affecting small business, and all business for that matter, which end result seems to be to lower productivity & raise prices.

Now we realize many of these problems are not under Congress's custody, or control.

Of the three above ① FHA & VA mortgages, ② zoning under regional government, and ③ high interest rates, the most serious & demanding of immediate solution is the high interest rates.

H. Ruppert & Son Well Co.
20420 CO. RD. #50 · HAMEL, MN 55340 · PHONE 425-3202

③

9-19-81

Hon. Vin Weber

Of course I'm speaking for the short term, as regional government has broad & frightening implications and effects already being felt.

High interest rates were mentioned by Pres. Reagan last week as beyond his control or influence. As I recall, he said only Congress has the ability to influence the Federal Reserve System, and we should be talking to our congressmen.

How can high interest control inflation when it's part of the problem?

How can small business keep prices lower when most are operating on a 3 to 6% net profit in normal times, and many are losing money now.

We realize everybody must suffer to get our economy back in line, but don't understand how high interest is doing anything but adding to the problem of inflation.

Again, we appeal to you for a solution to this disastrous situation.

Also, what is this doing to the independent bankers in our small towns?

Thank you,

Sincerely,

Anthony Ruppert

Kent E. Hopkins
LICENSED PUBLIC ACCOUNTANT
ROUTE 5, BOX 254
PRINCETON, MINNESOTA 55371

612/389-3500

September 19, 1981

The Honorable Vin Weber
Congress of the United States
House of Representatives
Washington, D.C. 20515

Dear Vin,

In reference to your letter about the impact of Todays interest rates on small business, I submit the following:

The high interest rates are good because they are discouraging consumer credit. People think twice before they buy non-essentials on credit or buy on bank loans. Also the encouragement has never been greater to save for the things they want.

But, the high interest rates are bad because my clients, who are all small businessmen, are having to limit production, lay off people and even close the doors because they are not profitable enough to pay the interest on additonal loans, or even existing high interest loans.

My suggestion is this: Keep interest rates high on loans for financing accounts receivable to discourage the expansion of ~~a~~ consumer credit and the purchase of non-essentials (such as consumer-goods: new cars, clothing, hardware, recreation equipment, etc.). But, reduce the interest rates on loans for capitol goods (which should be a natural because they can be more easily secured). This would apply to loans for putting up new buildings (homes as well) and buying equipment. We need the rates back in the 12% or under catagory to enable businessmen and homebuyers to borrow again for capitol goods.

I think you're on the right track, whatever you do, don't mandate an across the board cut in interest rates. This has been the problem in the past, they haven't stayed high long enough to change consumer physiology. We just need some adjusting now as to the areas we want to make low interest money ailable to. Anyhow, I think it can be done on a logical basis through our present banking system.

Sincerely
Kent E Hopkins

OLDSMOBILE

LOCKWOOD MOTORS, Inc.

1310 E. College Drive Telephone 532-2215
MARSHALL, MINNESOTA 56258

Cadillac

Sept 14, 1981

Congressman Vin Weber
House of Representatives
511 Cannon Bldg
Washington, D.C. 20515

Dear Congressman Weber-

In answer to your letter to me of Sept 14, 1981 asking how interest rates affect small business practices, I offer a simple example:

Because money costs are high, an auto dealer will not inventory as many vehicles; because not as many vehicles are in inventory, it will take less people to care for them (washing, inspecting, polishing, etc.) Therefore a dealer has no reason to hire additional people to create any more jobs.

The same can hold true for the dealers parts supply — If money costs are high (as they are) the dealer will not be likely to expand his parts inventory by stocking more parts. Therefore, he will need less people to handle the same parts — no additional hiring if he were to expand his parts operation.

In short, the volume of business will determine the number of jobs created!

Keep up the good work Vin!

Bob Lockwood

GM

Rt 1 Montrose, Mn.
Sept 20, 1981

Mr Weber,

I am writing to you in reply to the letter you sent.

This interest subject is a very touchy subject to me, And if it is going to continue at the rate it is I see there is no other way than the country to fall like it did in the 30's.

We have sold aur building of business but we are still trying to sell the machinery that we had on hand but nobody has the mony to buy And if they can borrow it, could not afford the 19% interest. If interest rate would not go over 12% I believe the economy would come back again And it would create work for people Like right now we would like to build a new home which would create work for people, but who can afford 19%. And I know how much interest to pay on a 19% loan as we had one and I thought it was terrible.

To me there are three things which aur bad for aur nation they are high interest And taxes and many people on Welfare.

As I stated before we sold aur building for the Machinery business Sales which will be a factory of Printers Ink. we felt that would be best to do as the sales dropped so much this year due to the money situation. and I do believe these problems will never be solved until the interest rate goes down.

Good luck at trying to achieve this as our nation really needs it.

Sincerely
Edith & Clarence Ouverson

ANDREWS AUTO REBUILDING
RT. 4, BOX 223
PRINCETON, MN. 55371

September 20, 1981

The Honorable Vin Weber
514 Cannon Bldg.
Washington, D.C. 20515

Dear Congressman Weber:

It is time that something is done to bring down the interest rates. As a small business, these interest rates are slowly but surely strangling us.

All small businesses from time to time have to borrow capital to stay in business. Many times to take advantage of volume buying so we are competitive with large businesses. Also at times like these, when everyone does not pay on time, when accounts receivable rise and it is necessary to increase and update equipment and inventory.

To borrow for these reasons has become difficult. To pay 20% interest to buy euipment needed for this new generation of cars is impossible. These interest rates take the profit out of using the new equipment. And without some of this equipment we'll not be able to do much of the frame work we do now and a portion of our business will be lost.

Volume buying to compete with larger competitors has come to an end for us. We cannot save enough now to offset the interest. If the interest is not changed so we can borrow money for short term situations, then we have lost to the big operators once again. We have to be competitive. Once we have lost that a small business is quickly another empty building, which we see so many of here.

And finally we see by our accounts receivable that everyone else is in the same situation. Customers and businesses that used to pay by the 10th of each month now pay, if we're lucky, by the end of the month or into the next month. In the past we borrowed money so that we could stay current with our creditors and level out our cash flow. At the current interest rates our profit is totally eaten up by interest, and we lose money. The result is that we cut off more business which doesn't get done or is taken to a large operation or a Detroit dealership which can carry these people for these short-term situations. Small businesses cannot operate without being able to use the banking system for short term financing.

Our business is unable to update, expand, or be competitive in the future without some help with the interest rates. Private sector jobs cannot be assured or new ones created with this type of atmosphere. The interest rate MUST be brought back under control.

Respectfully,

Charles Andrews

all
real estate, inc.

September 21, 1981

Congress of the United States
House of Representatives
Congressman Vin Weber
Washington, D. C. 20515

Dear Congressman Weber:

I appreciate the opportunity to express my opinions to the Sub Committee on Tax, Access to Equity, and Business Opportunities.

As a small businessman involved with a commercial real estate brokerage I find the extremely high interest rates to be a serious detriment to the normal operations of our business. However, the most devistating effect is being felt by the first and second time home buyer and the small real estate investor.

I agree with your opinion that high interest rates is one of the most complex problems facing the small businessman today. Regardless of the complexity and the political implications, the problem of high interest rates must be addressed honestly, and a serious attempt made to resolve the situation during this congressional session.

Many local businessmen, myself included, feel the problem was initially created by the Federal Government and as such therein lies the solution. Years of deficit budgeting to fund liberal spending programs has created an extremely competitive market for borrowed funds. The Federal Government has the edge in obtaining the needed funds over the private sector and the rates escallate along with the increased demand.

Total elimination or at least severe reductions in deficit spending would serve to remove the Federal Government from the market place. The interest rates would then be allowed to truly reflect the demand.

I realize that the budget cuts of any type are an extremely sensitive political issue. However, failure to take a responsible stand and face the problem realistically can only lead to further economic problems and continued escallation of interest rates. The end result will harm the very group that programs were formed to assist.

33-33rd Avenue, North / Village West Shopping Center
St. Cloud, MN 56301 / Telephone 612/253-7979

Congressman Weber
September 21, 1981
Page Two

On the local level high interest rates have had the most damaging impact on the residential real estate market. Personal home ownership has been a very achievable dream to the average American. The chance of that dream reality is rapidly fading. As interest rates escallate the average working consumer can no longer qualify for mortgage financing.

The continued inability to secure financing for private housing creates a necessity for rental units. As the demand increases and shortages are created, the insuing competition will continue to drive rental rates higher. If this situation is not reversed private housing in our nation will cease to exist except for a selected few.

Speculation in the real estate market, more specifically in residential housing, has had a great impact on the escallating price of a new home as well as rapidly rising rental costs. As the ability to secure affordable private housing is reduced due to higher interest rates demanded, the remaining units could increase and be far more inflationary than the current condition that the restrictive money policies are attempting to correct.

I have full confidence that the current economic problems facing our nation can be resolved. By putting personal political motivation aside and concentrating on resolving the problems for the good of the nation, a joint effort of the Executive and Legislative branches can complete the task at hand.

Sincerely,

Robert C. Abel

RC:dw

Karls Construction Co.
NEW HOMES • REMODELING [illegible]
Phone 252-3545
MEMBER OF CENTRAL MINNESOTA ASSOCIATION OF HOME BUILDERS

Sept 21, 1981

Representative Vin Weber
House of Representatives
Washington DC 20515

Dear Representative Weber:

When are you poeple in Washington going to do something about high interest rates? I've been in the home building business for almost 30 yrs and for the first time I'll be forced to lay all my men off. Not because of lack of work. I have several homes bid now that I Could start this fall, but people can't afford the interest.

The Federal Reserve says we'll drop interest when inflation comes down. How! they're the Cause of inflation. When I have to add $10,000.00

Karls Construction Co.
NEW HOMES & REMODELING [illegible]
Phone 252-3545

And more to the price of a home just to cover interest that's unneeded expense - inflation

When I and my men have to be out of work in another wk to 10 days - instead of paying over 500.00 in taxes we'll be collecting over 400.00 a wk in unemployment. That's a difference of over $300.00 per man per week. No wonder the federal government, and the states can't balance the budgets.

I think interest rates should be at a maximum of 10% and frozen from raising above that. Then tax anyone or company that makes excessive profits because of it which would cause inflation.

Sincerely,

Al Karls President
Karls Const Co

MATTSON
The Building Concept People

September 21, 1981

Honorable Vin Weber
Congress of the United States
House of Representatives
Washington, D.C. 20515

Dear Vin:

We do appreciate that you recognize that our biggest problem today, without a doubt, is high interest. Absolutely nothing else is holding our Industry back today. It is absolutely devastating and many, many of those in our Industry are going under. Something must be done.

Some, although very few, are building and paying 22% interest. They either are unable to realize the consequences of that usery rate or are in such a profit making business (not very many of these) that interest doesn't stop them.

Interest for our Industry must come down or there will be none of us left. A few of us that have really worked hard and who were fairly strong financially have been able to hang on, but those who weren't very strong could#stand up in this financial climate. And all those who were working for those Contractors are now without jobs or working in another Industry.

My partner and I made a vow a year plus ago that we would work hard to keep all our people and minimize our losses. So far we have managed to do this but we can't keep it up too much longer.

I made copies of your letter for some of our key people, especially Sales Representatives who have really been hurt by this, to put in writing to me just how high interest has effected them and those they are working with. They are out in the battlefield daily and know exactly what's going on. I thought they probably could do a much better job of giving the details to you Vin than I could so I have attached copies of what they wrote to me.

Thanks for anything you can and must do. Have a really good day and a Super-Great life.

Very Sincerely Yours,
Mattson Building Co., Inc.

Kale
Kale W. Danberg, President

Mattson Building Co., Inc. ■ Cokato, Minnesota 55321 ■ (612) 286-2151

MATTSON
BUILDING AND SUPPLY CO., INC.
COKATO, MINNESOTA
PHONE 612/286-2151 55321
METAL BUILDING DEALERS ASSOCIATION

September 21, 1981

Mr. Kale W. Danberg, President
Mattson Building Co., Inc.
Cokato, MN 55321

Dear Kale:

You have requested a comment from me on the impact high interest rates are having on current business practice.

As a building consultant for Mattson, I travel southern Minnesota and meet with small businessmen in all areas of endeavor.

Let me be emphatic: Interest rates have devastated the small business economy! Small business operations are by nature more risky than larger enterprises. High interest rates have provided for a money market that insures the investor of no risk. Why would anybody take a risk on making a loan to a small enterprise when seventeen per cent can be made without any risk at all. Let me share with you the details of two building projects on which I have worked recently.

Mr. N. is the owner of a small grocery store in a suburb of Minneapolis. He is sixty three years old and he has been in the grocery business for fifty years. For the past ten years he has owned and operated a corner grocery store successfully. His long range plan is to incorporate his business and bring in his four children as part of the ownership.

The city in which he is doing business will be building a road through the present site of his store. Mr. N. needs to rebuild his store on another site. The rebuilding project will cost approximately $250,000. Mr. N's business history, his part management practice, his experience and work history, his present balance sheet, all indicate that he would qualify for such a loan. That is--he would qualify for a loan if the interest rate was not at 22 per cent. Mr. N. will have to sell the most expensive bananas in the State of Minnesota to make back 22 per cent. Would Red Owl, Super Valu, Fairway Foods, make a loan at 22 per cent?

What advice would you give Mr. N?

Mr. V. is the president of a manufacturing plan that presently operates in 40,000 square feet. He would like to add an additional 20,000 square feet because he feels he can sell more than he is making. This expansion

Kale Danberg
Page two
September 21, 1981

would create from 10-15 new skilled labor jobs. When he computes the 12% to 15% money for which he is eligible into the price of his product, the expansion becomes less feasible. The result is that this fabricator of sheet metal products will not consider expansion at the present time.

In one instance we were able to find some 13% money which was available through some foreign source. We were later told their money might be illegal so we dropped negotiations.

What bothers me is that the 13% money is illegal, but the 22% money is legal. What kind of comment does this fact make?

Sincerely,

MATTSON BUILDING CO., INC.

Mike Olson

Mike Olson
Building Consultant

MO:js

MATTSON
BUILDING AND SUPPLY CO., INC.
COKATO, MINNESOTA
PHONE 612/286-2151 55321

September 21, 1981

Mr. Kale W. Danberg, President
Mattson Building Co., Inc.
Cokato, MN 55321

Dear Kale:

In my contacts with many different types of business I find that the owners are extremely discouraged because of:

1. High interest rates on mortgages;
2. High interest rates on operating capital.

Combine these two factors, and it becomes very difficult for a company to build at the present time, or expand their present facility.

Many of these companies are looking at their competitors, watching them "fall by the wayside", making them fearful of any new construction. Though they need a new building, they make do with the existing structure, rather than pay the high interest rates.

I feel any relief in this area through tax advantages, etc. would help immensely in stimulating the economy.

Sincerely,

MATTSON BUILDING CO., INC.

Rod Lund

Rod Lund
Building Consultant

RL:js

MATTSON
BUILDING AND SUPPLY CO., INC.
COKATO, MINNESOTA
PHONE 612/286-2151 55321

METAL BUILDING DEALERS ASSOCIATION

September 21, 1981

The Honorable Vin Weber
6th District Congressman
House of Representatives
Washington, D.C. 20515

Dear Mr. Weber:

The impact of existing high interest rates on America's small businesses has been a devastating one.

The greatest of American tragedies is that the constant overspending of our leaders has caused an artifically inflated interest rate that has been crushing to death many of our nation's small businesses.

These small businesses have been the backbone of our nation and now seem to be treated without reverence, or concern for their part in this great nation's future.

I sincerely hope you will do your best in supporting any legislation that would give America's small businesses a chance to regain their footing; for it is these very businesses that are the hope of America's future.

Sincerely,

MATTSON BUILDING CO., INC.

Bob Amiot

Bob Amiot
Building Consultant

BA:ja

MEMO

TO: Kale Danberg

SUBJECT: Reply to your note re. interest rates.

An obvious understatement is that current interest rates are too high. In rural areas it causes a tremendous burden on the farmer who requires large amounts of short term credit between planting and the time he receives cash for his crop. Even when weather is favorable and yields are high, allowing him to realize a small profit, if he anticipates that interest rates will still be high next spring, he will keep his spending to a mimimum. Worse yet, younger operators who must borrow heavily, will likely have a negative cash-flow even when the weather is favorable. Poor growing conditions often cause total disaster.

When the farmer is hurting financially, small business in rural towns and cities suffer dramatically. Sales for everyone from the implement and auto dealers to the small hardware store suffer. This means less employment, both full-time and part-time. The affect of these smaller pay envelopes trickles down through the whole local economy including finally the grocery and variety outlets.

Lighter pay envelopes and high interest rates have brought the new housing industry to a standstill in Cokato and elsewhere in Central Minnesota. This has set off another whole round of depressing circumstances causing still smaller payrolls and operating losses for local small business.

Our (Mattson Building Co.) bread and butter are medium sized commercial projects for small businessmen in rural towns and cities. With decreasing sales, operating losses, and the highest interest rates in the memory of most people, there is no way that the majority of the owners of small businesses can justify new construction at this time. For us this means operating losses, less employment, delayed wage and salary increases, fewer bonus' and a threat to our corporate existence.

Corporate losses, lighter pay envelopes, and decreased retail sales,all add add up to lower tax revenues, causing governments at the various levels to sop up an increasing percentage of funds available in the money market. Heavier government borrowing increases interest rates and starts the cycle all over again and adds fuel to the fire.

The only way to break the cycle and put out the fire is to decrease government spending and borrowing. A few painful first steps have been taken in this direction. More must be done. At this point, massive government loans to the private sector are not the answer. This will only feed inflation, increasing the cost of running a government, and causing governments to use up an even greater portion of limited funds available in the money market.

As government spending is brought under control, the Feberal Reserve should take steps to ease the interest rate with the hope of stimulating the economy. The timing and speed with which this is done must be left to the people with the expertise and who have available to them information and statistics necessary for prudent decisions in such far-reaching matters which affect all of us.

- Ed Dicke

ELECTRO INDUSTRIES, INC.
2150 W. RIVER STREET • MONTICELLO, MN 55362 • (612) 295-2500

September 21, 1981

Representative Vin Weber
514 Cannon Building
Washington, D.C. 20515

The Honorable Vin Weber:

In reference to your September 14th letter on high interest rates.

Our company has two primary product applications:

A. agricultural confinement building heating and ventilating controls.

B. residential electric heating for off peak rates and conversion of fuel oil furnaces to coal generated electric energy.

The following are some items indicating our business which we directly relate to high interest.

1. 1979 total sales 1.6 million, net income before taxes of $149,000.
2. 80% of the 79 sales were to our agricultural market.
3. 1980 sales 1.05 million, net loss of $49,000.
4. 44% of these sales were to the agricultural market.
5. According to the current year we will have sales of less than a million with 30% to the agricultural market.
6. The reduction is our agricultural sales is not necessairly due to depressed farm prices but there is no new construction, improvements or no new investment because of the high interest rates.

We sell our agricultural products directly to a marketing company, Aerovent Fan & Equipment of Lansing, Michigan. They are a very old line company and have had a very difficult time predicting and coping with the current situation. They believe the meat raising industry is in desperate trouble without investment and facility improvements.

By necessity of survival we had to invest highly with borrowed money in adding products and marketing strength to our second product area.

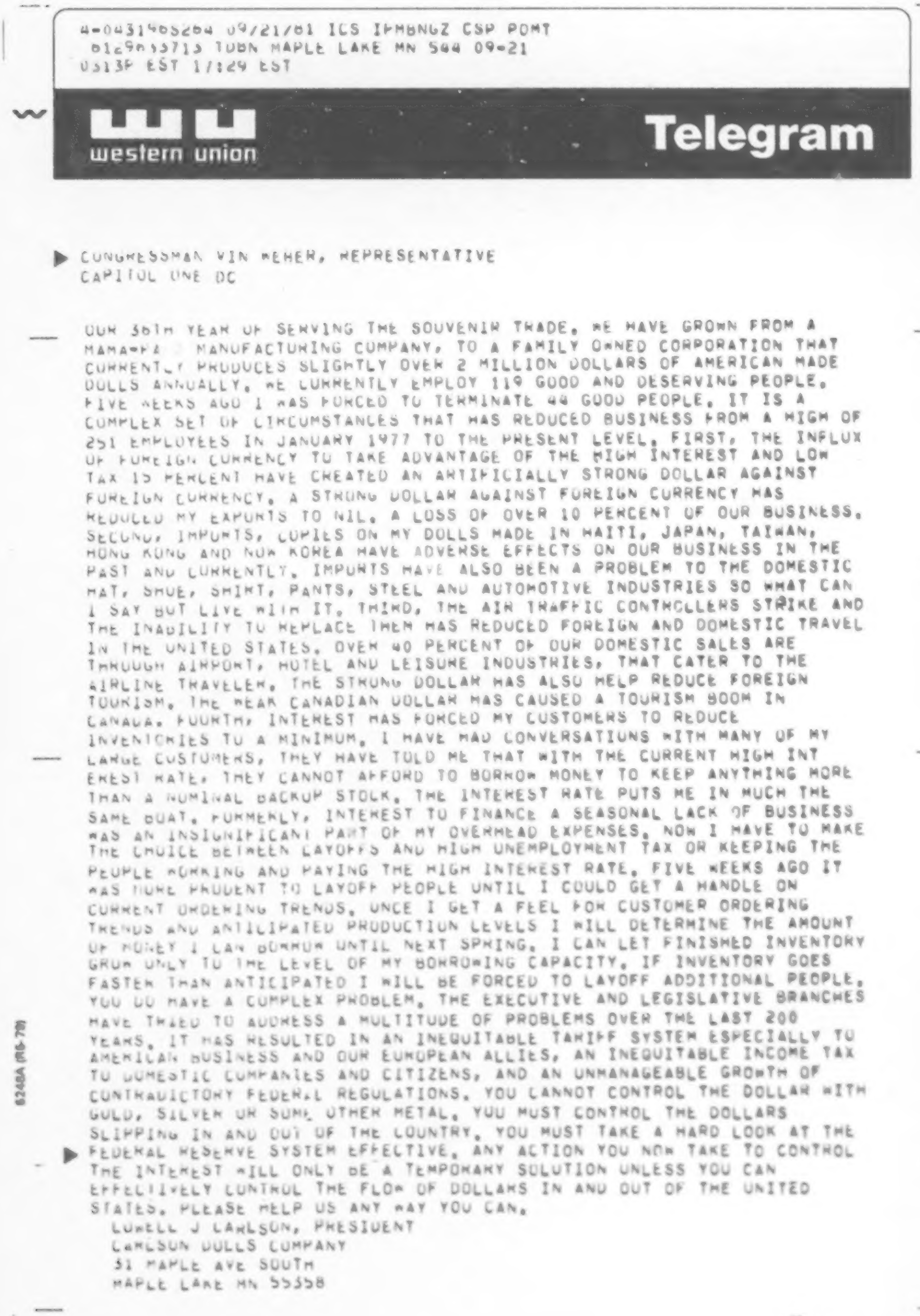
In 1979 our interest expense was $6,000. In 1980 our interest expense was $23,000, and this year it will probably be in excess of $50,000.

Thank you for your interest in our problems.

Sincerely yours,

William J. Seefeldt
President

mls



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western union Telegram

CONGRESSMAN VIN WEBER, REPRESENTATIVE
CAPITOL ONE DC

OUR 36TH YEAR OF SERVING THE SOUVENIR TRADE, WE HAVE GROWN FROM A MAMA-PA MANUFACTURING COMPANY, TO A FAMILY OWNED CORPORATION THAT CURRENTLY PRODUCES SLIGHTLY OVER 2 MILLION DOLLARS OF AMERICAN MADE DOLLS ANNUALLY, WE CURRENTLY EMPLOY 119 GOOD AND DESERVING PEOPLE. FIVE WEEKS AGO I WAS FORCED TO TERMINATE 44 GOOD PEOPLE, IT IS A COMPLEX SET OF CIRCUMSTANCES THAT HAS REDUCED BUSINESS FROM A HIGH OF 251 EMPLOYEES IN JANUARY 1977 TO THE PRESENT LEVEL, FIRST, THE INFLUX OF FOREIGN CURRENCY TO TAKE ADVANTAGE OF THE HIGH INTEREST AND LOW TAX 15 PERCENT HAVE CREATED AN ARTIFICIALLY STRONG DOLLAR AGAINST FOREIGN CURRENCY, A STRONG DOLLAR AGAINST FOREIGN CURRENCY HAS REDUCED MY EXPORTS TO NIL. A LOSS OF OVER 10 PERCENT OF OUR BUSINESS, SECOND, IMPORTS, COPIES ON MY DOLLS MADE IN HAITI, JAPAN, TAIWAN, HONG KONG AND NOW KOREA HAVE ADVERSE EFFECTS ON OUR BUSINESS IN THE PAST AND CURRENTLY. IMPORTS HAVE ALSO BEEN A PROBLEM TO THE DOMESTIC HAT, SHOE, SHIRT, PANTS, STEEL AND AUTOMOTIVE INDUSTRIES SO WHAT CAN I SAY BUT LIVE WITH IT, THIRD, THE AIR TRAFFIC CONTROLLERS STRIKE AND THE INABILITY TO REPLACE THEM HAS REDUCED FOREIGN AND DOMESTIC TRAVEL IN THE UNITED STATES. OVER 40 PERCENT OF OUR DOMESTIC SALES ARE THROUGH AIRPORT, HOTEL AND LEISURE INDUSTRIES, THAT CATER TO THE AIRLINE TRAVELER. THE STRONG DOLLAR HAS ALSO HELP REDUCE FOREIGN TOURISM. THE WEAK CANADIAN DOLLAR HAS CAUSED A TOURISM BOOM IN CANADA. FOURTH, INTEREST HAS FORCED MY CUSTOMERS TO REDUCE INVENTORIES TO A MINIMUM, I HAVE HAD CONVERSATIONS WITH MANY OF MY LARGE CUSTOMERS, THEY HAVE TOLD ME THAT WITH THE CURRENT HIGH INTEREST RATE, THEY CANNOT AFFORD TO BORROW MONEY TO KEEP ANYTHING MORE THAN A NOMINAL BACKUP STOCK. THE INTEREST RATE PUTS ME IN MUCH THE SAME BOAT. FORMERLY, INTEREST TO FINANCE A SEASONAL LACK OF BUSINESS WAS AN INSIGNIFICANT PART OF MY OVERHEAD EXPENSES, NOW I HAVE TO MAKE THE CHOICE BETWEEN LAYOFFS AND HIGH UNEMPLOYMENT TAX OR KEEPING THE PEOPLE WORKING AND PAYING THE HIGH INTEREST RATE, FIVE WEEKS AGO IT WAS MORE PRUDENT TO LAYOFF PEOPLE UNTIL I COULD GET A HANDLE ON CURRENT ORDERING TRENDS, ONCE I GET A FEEL FOR CUSTOMER ORDERING TRENDS AND ANTICIPATED PRODUCTION LEVELS I WILL DETERMINE THE AMOUNT OF MONEY I CAN BORROW UNTIL NEXT SPRING, I CAN LET FINISHED INVENTORY GROW ONLY TO THE LEVEL OF MY BORROWING CAPACITY, IF INVENTORY GOES FASTER THAN ANTICIPATED I WILL BE FORCED TO LAYOFF ADDITIONAL PEOPLE, YOU DO HAVE A COMPLEX PROBLEM, THE EXECUTIVE AND LEGISLATIVE BRANCHES HAVE TRIED TO ADDRESS A MULTITUDE OF PROBLEMS OVER THE LAST 200 YEARS, IT HAS RESULTED IN AN INEQUITABLE TARIFF SYSTEM ESPECIALLY TO AMERICAN BUSINESS AND OUR EUROPEAN ALLIES, AN INEQUITABLE INCOME TAX TO DOMESTIC COMPANIES AND CITIZENS, AND AN UNMANAGEABLE GROWTH OF CONTRADICTORY FEDERAL REGULATIONS. YOU CANNOT CONTROL THE DOLLAR WITH GOLD, SILVER OR SOME OTHER METAL, YOU MUST CONTROL THE DOLLARS SLIPPING IN AND OUT OF THE COUNTRY, YOU MUST TAKE A HARD LOOK AT THE FEDERAL RESERVE SYSTEM EFFECTIVE, ANY ACTION YOU NOW TAKE TO CONTROL THE INTEREST WILL ONLY BE A TEMPORARY SOLUTION UNLESS YOU CAN EFFECTIVELY CONTROL THE FLOW OF DOLLARS IN AND OUT OF THE UNITED STATES. PLEASE HELP US ANY WAY YOU CAN,

LOWELL J CARLSON, PRESIDENT
CARLSON DOLLS COMPANY
31 MAPLE AVE SOUTH
MAPLE LAKE MN 55358

6248A (R6-70)

The Hutchinson Agency

Real Estate & Insurance

607 2ND ST. JACKSON, MINN. 56143

PHONE (507) 847-2160

September 21, 1981

Representative Vin Weber
514 Cannon Building
Washington, DC 20515

Dear Congressman:

Your letter of September 14th arrived a little late, but I still wanted to write as per your request, giving my opinion as to the impact of interest rates on current small business practices.

Although my business is very small, I am working with a number of firms that are involved to a larger scale than myself. Every one of these firms are feeling a drastic effect with the current high interest rates that are being charged by the Federal Reserve System at this time. Although the intent of high interest is to stop this inflationary period of time, it is having a drastic effect on the sale of houses and is a pyramid effect to the younger citizens endeavoring to make a start at this time. Currently, businesses that have to pay fifteen to twenty percent for a bank loan, when they only have only a twenty five to thirty percent margin to work on, is again taking it's toll in the number of businesses that are currently being forced out of operation.

Again, relative to the real estate business, the savings and loans are in dire financial trouble, due to paying high interest rates on savings accounts and having an old portfolio of small interest rates, coupled together with a decrease in a number of new loans to increase their portfolio. Three large mergers have recently occurred and undoubtedly there will be more to follow, if this trend continues.

It is my opinion, that if this interest rate continues at today's high level, there will be no choice, but we will be in for a major recession, because the backbone of this country is still based on small businesses that cannot stand the current high interest rates, without further failures occurring.

In face of the government cutting back on expenditures, which is an absolute necessity, wage increases are starting to effect the consuming public to the point where they can no longer afford these products. Couple high interest together with further increases in wages, and again we are going to have a disastrous effect, in my opinion.

My statement is brief, but I think it will give you my opinion, and if I can help further, please advise.

Very truly yours,

Jack

Jack C. Hutchinson

b

VOIGT'S BUS SERVICE INC

GENERAL OFFICE:
Route 3
St. Cloud, Minn. 56301
Phone (612) 252-1807

September 21, 1981

Congressman Vin Weber
514 Cannon Building
Washington, D.C. 20515

Dear Sir:

In response to your letter of September 14, 1981, I agree with you thoroughly that the matter of the impact of high interest rates on small business activities is indeed most important as well as being frustratingly complex. In our own experience, in the wake of agonizing analysis, we have, of necessity, had to defer indefinitely any thought of even a modest growth in our fleet or facilities. In terms of dollars, we were talking about something around the 1/2 million mark--but at current money cost, we simply can't afford such an expenditure.

I recognize that these numbers are miniscule by comparison with the consideration that larger businesses must face, but there-in lies the real importance of the matter: and that is that these "miniscule" numbers multiplied by the number of small businesses "in the same boat" as we are, so to speak, represent, in total, staggering deferral of capital goods purchasing, plant expansion, improvement--all to the great detriment of the total economy.

Now, having said this, I confess that it hasn't helped one whit to solve the basic problem. I do think, however, that the Administration must be made to recognize that the devastating effect of high money cost upon "small business" in particular, is directly related to the excessively high level of Federal spending. The concepts of job creation, business revitalization, even sustaining business at reasonably viable levels in current status, are of little meaning, otherwise.

Sincerely,

G. T. Odenbreit

G. T. Odenbreit
General Manager

GO:ck

TRAVEL AS A GROUP—CHARTER A BUS FROM US

Modern Trailer Sales & Service, Inc.
218 U.S. HWY. 52
TEL: 612/426-8000
OSSEO, MN 55369

September 21, 1981

Congressman Vin Weber
Congress of the United States
House of Representatives
Washington, D.C. 20515

Dear Congressman,

Thank you for writing to me about the small business man and his problems. I will try to give you an idea of how we are affected.

High interest rates are the biggest problem facing our dealership today. We have both retail financing and inventory floor planning problems.

With inventory financing at 1.75% over the prime interest rate, we have had to lower our inventory from approximatly $500,000 to 300-350,000. We can't get the sales volume up to a level that we have enjoyed and been accustomed to. The energy situation of 1979 forced us to lay off half of our sales force, but because of our reduced volume we can't justify replacing these people. We have watched our annual gross sales drop from 3.0 million to 1.5 million. We are still profitable, but the drop in sales is a hard bullet to bite at a time when other aspects of the business look good.

Our Retail financing has also hurt us. We can't legally charge over 16.66% interest on a 7 year contract. The lending institutions want 18%. We have to make up the difference. This is a state inflicted problem, but if the interest rates weren't so high we wouldn't have to be confronted with having to pay these extra fees.

We realize we didn't get into this mess over night, and its going to take a while to get back out, but picking up the morning paper and reading that the prime dropped 1/2% is a good day brightner.

Thanks for keeping in touch.

Sincerly,

Bill Borry

Bill Borry
President, Modern trailer Sales

September 21, 1981

Dawn Blomgren
Blomgren Trucking
R.R. 2
Tyler, Minnesota 56178

Dear Honorable Vin Weber,

I am writing this letter on behalf of my parents, who own and operate a trucking business.

In regard to the up coming hearings by the Small Business Subcommittee on Tax, access to Equity Capital and Business Opportunities, I would like to express my opinion on the problems caused by high interest rates.

Because of the excessively high cost of borrowing money, small businesses are unable to come up with the capital to purchase new or replacement equipment. We are also unable to expand our business which means we are unable to offer any new job opportunities.

This is going to cause a much more complex problem down the road a few years, because as equipment wears out, how are we going to replace it? Does this mean that many of the small businesses will have to go bankrupt or discontinue operations and be taken over by the larger corporations? Large corporations are able to secure financing through various stock options. This is an option which is not fiesable for indurdual small businesses or farmers.

I feel that if money were available at reasonable interest rates, many

Small businesses would purchase new equipment and/or increase their number of employees. I also feel that if money were available, many new enterprises would be started.

Why doesn't the government work on programs to help more and more people become employed or start businesses rather than offering more and more social benefits for people that are unemployed?

Why isn't something done so that family businesses may be passed on from one generation to the next without beg eaten up by inheritance taxes?

A strong growth rate in small businesses would have an immeasurable impact on the nations economy. It would create thousands of new jobs, many new and useful products and much tax revenue, both state and federal. Creating new jobs and new products would immensely improve the attitude of the American people because they would feel they were accomplishing something instead of just being a number in the unemployment or welfare line.

I am a senior at Russell-Tyler High School and I really wonder what the future is going to hold for us. Will there be job opportunities? Is it worth while to persue futher education? There are now many people in the job market that have post high school education and are over qualified for the jobs presently available.

Many of these problems would be corrected if small businesses were not over taxed and regulated and had working capital available.

Thank You
Sincerely,
Dawn Blomgren
Blomgren Trucking
RR 2
Tyler, Minnesota 56178

D.H. BLATTNER & SONS, Inc.
CONSTRUCTORS
AVON, MINNESOTA 56310

September 21, 1981

Vin Weber, Congressman
6th District, Minnesota
514 Cannon Building
Washington, D.C. 20515

Dear Sir:

The construction industry is a most competitive industry. Profit margins are slim to none, especially during the past few years. We have no room for unproductive cost increases.

Interest, it is an unproductive cost. In order to do business you must have money, and in the private sector your only source of funds are plant and working capital borrowing.

Interest expenses have doubled our total overhead costs, have wiped out any thoughts of purchasing new equipment and completely eliminated our slim profit margins.

We have to borrow money and when interest rates are able to move from 12-22% it disrupts our planning, eliminates jobs and keeps us from purchasing new equipment.

Very truly yours,

D.H. Blattner & Sons, Inc.

S.C. Blattner, Secretary

SB/cr

"An Equal Opportunity Employer" PHONE (612) 356-7351

RCA **UPHOFF GAMBLE STORE** Whirlpool
Avon, Minnesota 56310
Whirlpool & Coronado, Speed Queen Appliances
RCA TV Plumbing and Heating Bottle Gas
Service & Repairs
Phone 356-7535

9-22-81

Dear Congressman Weber:

Small business like the small farmers are in trouble. I'am in the hardware business. Last year my gross was 120.000 thousand. Cost to run a business is way out of line. Government regulation drive you nuts. Interest is dam high you can't afford to borrow. Last week I borrowed money at my local bank I paid 18½ %. I had to borrow as I was several month behind on my mortages or close the door. If things don't get better by winter I'll close anyway. I had my place for sale for a year & half already. I had buyers but no money. Some a little down payment, but the bank said no, as interest would eat them up on the balance. Big business is just plain & simply eating us up. I'am the only hardware store in town & still can't make. The city has 850 people & 1500 around our lake & outside of town. I'am always short of capital, never anything left to increase my inventory. If I had a bigger inventory & some money to play with I could make it. Is there any help for us to borrow at a lower rate for a longer time. Interest & taxes take all I have. My wife has worked for 17 yrs, with out her income taking care of the house, I wouldn't be here. I'am in business here for 31 years & last four years I borrowed to stay in business. If I don't sell soon I close the door & Avon has no hardware store. The only ones that can keep going in this town is the grocery stores & the bars. At one time I had six employed, now I'am down to one part time student.

RCA **UPHOFF GAMBLE STORE** Whirlpool
Avon, Minnesota 56310
Whirlpool & Coronado, Speed Queen Appliances
RCA TV Plumbing and Heating Bottle Gas
Service & Repairs
Phone 356-7535

Keep Controls on Natural Gas.

If its decontroled, the same will happen as it did to fuel oil. There's plenty gas, so keep the price down. If prices go up who get the stab in the back. The poor people. Look what fuel assistance is costing us already & what will it be if controls go of gas. / Keep the lid on natural gas

Vin, I saw in the paper where you are in favor of high interest. Why is that. You must have plenty money & on interest to be in favor of it. Look at all the people out of work just in the Construction business alone. Why aren't they building, interest to high. It put the carpenter, brick layer, electrician, plumber, rug layer, cabinet maker & right down the line out work. This is just Construction because of the high interest. Lets get interest down, people back to work -

(unions.) I'am no union man. Regan firing the Controlers was the best thing that could of happened & I sure hopes he sticks with it. State employees working in hospitals where lives are involved shouldn't be allowed to strike. The dollar is there life & not the human being its sad. How would you feel if you were deathly sick in a hospital & no employee around to take care of you. Think about this. I'll work for the state if I could get hired for the money they're getting. I don't make that in business.

Yours truly
Wessl Uphoff

UPHOFF GAMBLE STORE NO. 5731
107 AVON AVENUE SOUTH
AVON, MINNESOTA 56310
TELEPHONE: 356-7535

UPHOFF GAMBLE STORE NO. 5731
107 AVON AVENUE SOUTH
AVON, MINNESOTA 56310
TELEPHONE: 356-7535

9-23-81

Dear Congressman Weber:

(Lets do something About High Interest Rates)

High interest rates are hurting millions of american families, business and industries. Homes aren't being built because potential buyers can no longer afford today's exorbitant interest rates. Automobiles an other Consumer needs are going unsold for the same reason. People are losing jobs as business sags. Savings are vanishing. Government is losing tax revenue, as more jobs disappear and profits dip. Personal & business bankruptcies are high.

Something, obviously, has gone wrong. If you have to kill the patient to stomp out the disease, then its time to try a new treatment. Each day that interest rates go unchecked, more jobs are lost & more people suffer.

For millions of americans, there is little time left. For many its already to late.

Now is the time to take bold steps. Do something today & not tomorrow.

Yours truly
Jess Uphoff

SEPTEMBER 23, 1980

MR. VIN WEBER
514 CANNON BUILDING
WASHINGTON, D.C. 20515

VIN,

ITS NICE TO GET CORRESPONDENCE FROM YOU REGARDING THE SMALL BUSINESS COMMITTEES. I HOPE MY THOUGHTS WILL HELP IN SOME DECISIONS ALONG THE PATH. FIRST OFF, MY COMPANY HAS JUST PASSED ITS FIRST YEAR IN BUSINESS, AND I MIGHT ADD IN THE RED. IF IT HAD NOT BEEN FOR MY PERSONAL SAVINGS TO INVEST TO START THIS BUSINESS IT WOULD HAVE NOT SURVIVED THROUGH A LOAN SITUATION IF THAT HAD BEEN THE CASE. BECAUSE OF HIGH INTEREST RATES AND THE LACK OF CAPITAL TO INVEST FOR EXPANSION IT IS IMPOSSSIBLE FOR THE SMALL BUSINESS I'VE STARTED TO EXPAND AND CREATE MORE JOBS FOR EMPLOYEE'S. AT THIS TIME I CAN VISUALIZE A NEW BUILDING IN THE NEAR FUTURE, BUT NOT AT 20% INTEREST AND 30% DOWN. THE TAX LAWS REQUIRED BY THE FEDERAL GOBERNMENT WILL NOT ALLOW US TO INVEST IN MACHINERY, BECAUSE OF THE TAX ON EBD OF THE YEAR PROFITS. I'M BUT YOUNG IN THIS BUSINESS AND CANNOT EXPECT A WHOLE LOT IN ONE YEAR. OUR GROWTH HAS BEEN OVER 700% SINCE LAST YEAR WHICH IS ENCOURAGING. BUT OUR CASH FLOW IS ANOTHER STORY. LETS LOWER THOSE INTEREST RATES SO WE HAVE MORE BORROWING POWER. I'M sure YOU'VE HEARD THIS STORY MANY TIMES NOT ONLY FROM OUR TYPE OF BUSINESS BUT ALSO FROM THE FARMERS. BUT I HOPE THIS WILL REASSURE YOUR THOUGHTS, THAT WE HAVE NOT GIVEN UP ON THE FEDERAL GOVERNMENT OR THE PEOPLE.

SINCERELY,
AMERICAN TIME AND SIGNAL
J Baumgartner
JEFFREY RAY BAUMGARTNER
PRESIDENT

American Time & Signal
Co.

351 Atlantic Ave
P.O Box 407
Dassel, Minn.
55325

Redwood Falls, Minn
September 24, 1981

Hon. Vin Weber
514 Cannon H O B
Washington, D. C. 20515

Dear Congressman Weber:

Some of us never earned a lot of money in our life time but were conservitive and saved a few hundred dollars when ever we could. Over the years, even at 4 % and 5% interest it did add up to a fair sum of money. During these years we were being laughed at and called fools by the "wheeler-dealers" who bought everything they could get their hands on with the idea of borrowing cheap money and paying it off with cheaper dollars. Now that their plan isn't working they are the ones that are doing all the screaming.

I agree with the Federal Reserve Board and Paul Volker. What is wrong with letting interest rates seek their own level? Congress has no business what ever in trying to regulate interest rates. All that will result will be a bigger mess than we have now.

I think we who have saved a little money for the past 30 years are entitled to a good rate of return to help beef up our Social Security.

When are we going to stop the democrates from using the Social Security system to buy votes, and in the process demolishing the system for their own selfish political gain.?

Social Security is a program that my employeer and myself have contributed to for the past 43 years. Why is it classed along with food stamps, school lunch, and all the rest of the give away welfare programs, and why are these welfare programs called entitlement programs.?? The recipients of these benifits never contributed one red cent to these programs.

Very truly yours

Percy M Brandt

Percy M. Brandt.,
321 East Broadway
Redwood Falls,
Minnesota. 56283

JACK FROST, INC.

Minnesota Fresh Gold'n Plump Fryers & Eggs

September 24, 1981

Congressman Vin Weber
Congress of the United States
House of Representatives
514 Cannon Building
Washington, D. C. 20515

Dear Vin:

I am pleased to respond to your request of an evaluation of the impact of high interest rates on our business. Unfortunately your letter arrived too late to make the September 22nd deadline.

Yes, Vin, interest rates at the current level are hurting, but I would like to put the problem in perspective. Given the pattern of inflation the past year, and to the credit of the administration, Congress and the Fed, the inflation is starting to moderate, the most we could have hoped for was a 5 percentage point reduction in our working capital loan. This would have reduced our cost of dressed chicken by 1/3 of a cent per pound. Substantial, yes, since the Ag Business is a low margin business at best. Still in my view this is a small price to pay for some material progress in reducing inflation and at least now we have a hope of a brighter economic picture in the future.

Inflation, in its three faces, real current inflation, perceived current levels of inflation by the American public, and future expectations of inflation have been and still are the greatest threat to our nation. As we have discussed in the past, inflation is the result of 20 years of misguided fiscal and monetary policy. Can you blame the American public for not immediately dropping their expectation of future inflation when we have several months of some movement in a downward direction? The perceived rate of current inflation is also falsely signaled by the grossly erroneous way in which we measure the impact of rising prices on peoples lives. The ballooning of the C.P.I. due to the assumption everyone buys a new home and takes out a new mortgage each month as well as the inability to reflect substitutions or changes in buying habits has tended to reflect an upward bias to the C.P.I. of from 1 to 3 percentage points during the past several years. When Social Security, government pensions and the cost of living clauses in wage contracts are so directly indexed to the C.P.I. we actually fuel inflation with an over-stated C.P.I. Since expectations of future inflation is in my view the dominant factor governing long term interest rates, it behooves us as a nation to remodel the way we measure our inflation. I would hope sentiment would develop in favor of substituting another commonly used measure of price impact - namely "personal consumption expenditures".

It is always convenient to have a scapegoat for a difficult problem. Unfortunately the Fed today is becoming a popular whipping boy. In my view the Fed has done an outstanding job of controlling money suppply the past year. By focusing on the level of reserves in attempt to balance the growth of the various M's to meet their stated

309 Lincoln Ave. S.E. • St. Cloud, MN 56301 • Phone 612-251-3570

target, they are doing what they should be doing. The Fed should not be focusing on interest rates. Their first and foremost responsibility is to control the supply of money and credit to both encourage and reflect a gradual reduction of inflation over many years. To achieve their stated targets, they must be constantly adding and withdrawing reserves in response to the ebb and flow of commercial balances. In this light Vin, I was disappointed to see your latest mailer and the manner in which you criticized the Fed. In my view, your comment about Fed manipulation was unfortunate and only serves to undermine public support for monetary restraint and reduction of inflation. Is there really a policy action available to either Congress, the Fed or the administration that would reduce interest rates? I grant it is possible that a rapid increase in the money supply could, for a few weeks, drop interest rates but the ultimate result after a few months would be disaster in the form of even higher rates and erosion of whatever confidence in the future has been developed. In my view the looming federal deficit and all that portends for the credit markets is the principal reason interest rates have remained stubbornly high. I have enclosed a data sheet from a talk Volker made showing the combined effect of low savings rates in the U.S. and great amount of available capital that is soaked up by financing the federal deficit out of available market place funds. Some contend that we should print money to monetarize the deficit but to the extent we do, we again fuel inflation. Interest rates, I feel, are a mixture of supply and demand forces against a background of inflationary expectations.

Policy options then tend to fall in three areas:

one: add to supply: print money or encourage savings.

two: reduce demand: less Federal deficit and/or reduced private demand through a soft economy or targeted legislation.

three: reduce inflation and the expectations of future inflation.

In view of the high percentage of new capital that is being consumed by the Federal government and the difficulty in reducing the deficit, I would hope that sentiment would increase in Congress to reduce substantially the defense budget. I have to feel that this in the final analysis is the least risky policy alternative.

I would even encourage a delay of the July, 1982 tax cut to build revenues, and I don't think Social Security should be sacrosanct. Other methods of reducing demand could be legislated, such as limitation to deduction of interest on homes - particularly second homes, a limitation to consumer credit, elimination of IRB's, a minimum down payment on consumer credit. I agree these policy actions are all unpopular and probably politically impossible, but if you are to free capital for new P C E without reducing further the Federal deficit, then these are some legislative alternatives to consider.

On the supply side, we must recognize that returns on savings that reflect higher than traditional inflation premiums do serve to encourage saving. Maybe more could be done legislatively to provide additional incentives to savings - the problem is of course this cuts into revenues.

In the final analysis it seems that "quick fix" schemes to lower interest rates by browbeating the Fed and Wall Street or congressional credit manipulating are doomed to create far greater problems than they solve. My prescription - unimaginative, I agree, but best for the long run.

1. Support of Federal Reserve policies of monetary restraint with expectations that the Fed meet their growth targets for the various M's.

2. Much greater reduction and delays in defense budget expenditures.
3. Further but not devastating cuts in Federal budget items.
4. Further reduction in entitlement programs but again not drastic cuts.
5. Remodeling of our index of inflation or change to P C E.
6. Delay the effective date of July tax cuts to boost revenue.
7. More active selling effort on part of the President to reaffirm Reagonomics.
8. Patience on part of Congress and the American public. (Don't ask me how to accomplish this).
9. Further legislation late this fall or next spring to stimulate savings.
10. Pray

Well, Vin if you've had the patience to wade through all this ramblings, you're well conditioned to be patient on Reagonomics. It would be good to talk personally at some future time. Call me if your schedule has an opening.

Sincerely,

Don

Don Helgeson

DH/mr

Table 1

SOURCES OF SAVING IN THE UNITED STATES
(National Income and Product Accounts Basis)

	1975-79		1980	
	Billions of dollars	Percent of GNP	Billions of dollars	Percent of GNP
Gross national saving[1]	353.3	18.1	457.2	17.4
Capital consumption	201.0	10.3	287.2	10.9
Net national saving[1]	152.3	7.8	169.9	6.5
Personal	82.7	4.2	101.3	3.9
Corporate	47.0	2.4	44.3	1.7
Other	22.6	1.2	24.3	.9
Memo:				
Federal government deficit[2] (unified plus off-budget)	-60.9	-3.1	-83.3	-3.2

1. NIPA gross saving excluding NIPA federal surplus (or deficit) plus net foreign investment (sign reversed).

2. The federal deficit on an NIPA basis averaged $42.6 billion in 1975-79, 2.2 percent of GNP, and was $61.2 billion in 1980, 2.3 percent of GNP. The off budget deficit, alone, averaged $9.7 billion in 1975-79, and was $15.4 billion in 1980.

SOURCE: U.S. Department of Commerce, Bureau of Economic Analysis, National Income and Product Accounts. All rates are calculated as the average value of item for the period, divided by the average value of GNP. Details may not add to totals because of rounding.

Table 2

INTERNATIONAL COMPARISONS OF SAVING
(U.N. System of National Accounts Basis)

	1975-1979 Average	
	Gross Saving	Net Saving[1]
	--Percent of gross domestic product--	
Canada	20.8	10.1
Japan	32.0	19.0
France	22.8	11.6
Italy	22.2	12.2
Germany	23.0	11.8
United Kingdom	18.0	6.8
United States	17.2	4.9

[1] Gross saving less capital consumption allowances.

SOURCE: Organization for Economic Cooperation and Development, National Accounts of OECD Countries, 1962-1979 (Volume II). All country data are reported according to the United Nations System of National Accounts, which differ from the United States NIPA. Details may not sum to totals because of rounding.

Sept. 27, 1981

Congressman Vin Weber
514 Cannon Building
Washington, D.C. 20515

Dear Congressman Weber,

My name is Robert R. Olsen from St. Cloud, Minnesota.

We sold our home on October 3, 1980. Interest rates on home mortgages were 10-11% at that time. We completed building our new home on March 1, 1981. VA interest rates were 14% plus points at that time so we obtained a 3-month note hoping rates would decrease. We are currently paying 18½% on the present note. Eventually, we may have to sell our home or lose most of the equity we gained from the sale of our old home.

Why was the spread between the prime rate and the consumer index 12 points last month?

My wife and I are 49 years of age and *were* considered middle income people. We are asking for your help in lowering the *interest rate* situation.

Sincerely,

Robert R. Olsen
1810 11th Ave. S.E.
St. Cloud, MN. 56301

Robert R. Olsen, Counselor
STUDENT PERSONNEL OFFICE
Area Vocational Technical Institute
1540 Northway Drive
St. Cloud, Minnesota 56301

State Bank
OF REDWOOD FALLS
P. O. BOX 459
REDWOOD FALLS, MN. 56283
PHONE 507/637-2961

September 28, 1981

Honorable Vin Weber
514 Cannon Building
Washington, D.C. 20515

Dear Vin,

I am sorry I had not responded to your letter of September 14, 1981 concerning interest rates. However, I was hospitalized a few days and upon getting back to work I notice you requested the information be submitted to your office by September 22nd.

Coming from the banking community, I am not too sure that the words I have to say would be considered in the right context. There are many people in this country who feel that bankers prefer high interest rates; however, I am not one of them. The fact of the matter is that the bank operates on a "net interest margin" and as such would prefer the interest rates to be lower, both on the paying end and the receiving end. What I am trying to say is that if we have to pay 14 to 16% interest on the savings in the bank, we also have to charge 19 to 20% in order to pay the overhead expense, pay the interest due, and all of the other expenses that are incurred in the banking business.

The problems that exist in small business because of high interest rates are numerous. The automobile dealers are having a very difficult time because the people are not willing to buy automobiles and pay the high interest rate. Secondly, if the dealer has to floor plan a $10,000.00 automobile for six months he automatically has another $1,000.00 bill added to the car. Someone has to pay this. We have a manufacturing firm in town that is practically at a standstill. None of the dealers will carry any inventory. They refuse to carry inventory because they have to finance it and do not want to do so at the prevailing rates.

I do realize that this is a problem that is not easily solved. We cannot live with an 18 to 20% inflation rate either. This is one of the reasons I hope that President Reagan will not back down on his various programs for the economy. We are finally making some steps in the proper direction and need to continue this present course. I realize that there are a lot of people in the great United States that are hollering "Foul" but there are still many of us that want to see the present budget cutting and tax lowering continued.

I did read one news item a couple of weeks ago where a senator was thinking about legislating a "windfall profits tax" on banks. This is quite ridiculous since our profit is no greater at high interest rates than it is at low. We do calculate margins and I personally would prefer to see lower rates.

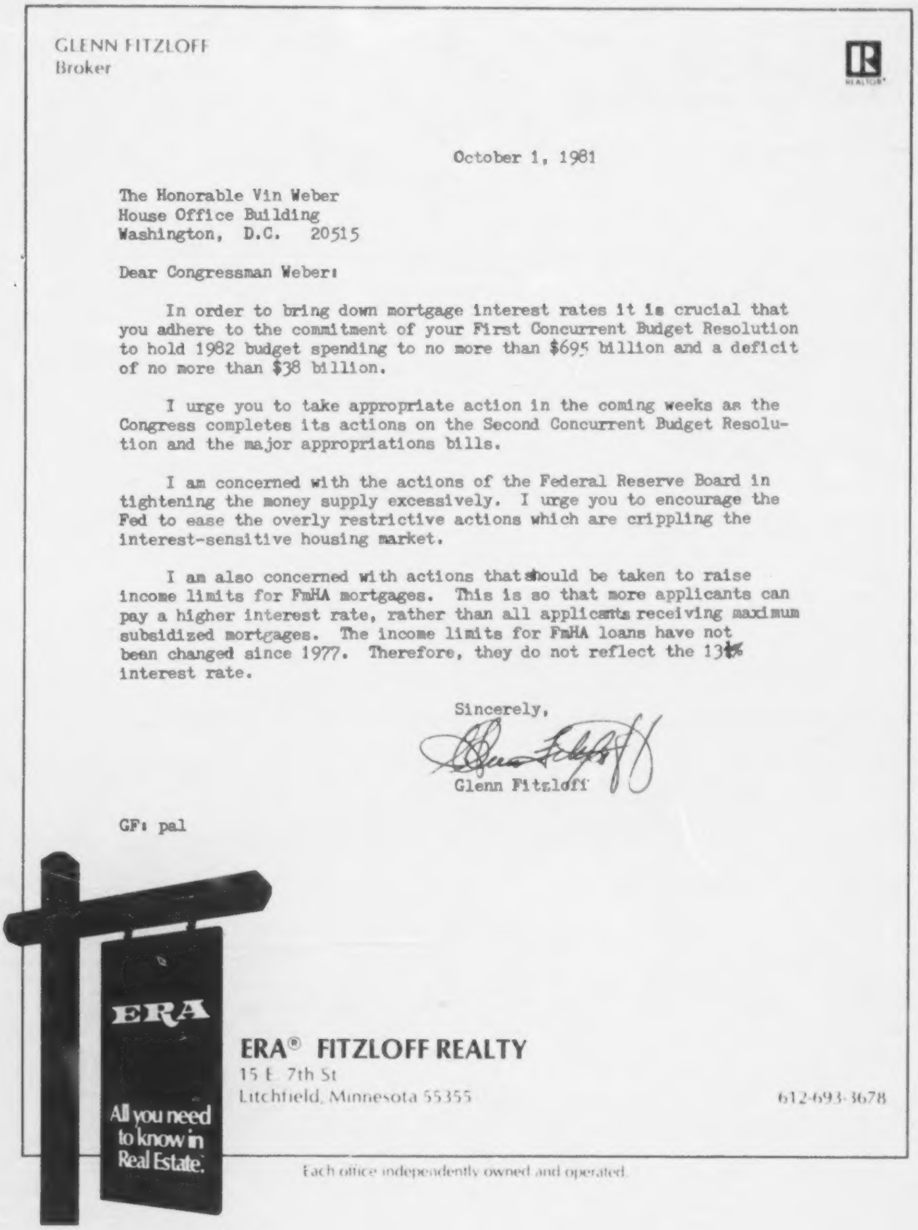
Although this letter is a little late, I do appreciate the opportunity to sound-off.

Sincerely,

Pete

L. K. Iverson
President

LKI:dh



GLENN FITZLOFF
Broker

REALTOR®

October 1, 1981

The Honorable Vin Weber
House Office Building
Washington, D.C. 20515

Dear Congressman Weber:

In order to bring down mortgage interest rates it is crucial that you adhere to the commitment of your First Concurrent Budget Resolution to hold 1982 budget spending to no more than $695 billion and a deficit of no more than $38 billion.

I urge you to take appropriate action in the coming weeks as the Congress completes its actions on the Second Concurrent Budget Resolution and the major appropriations bills.

I am concerned with the actions of the Federal Reserve Board in tightening the money supply excessively. I urge you to encourage the Fed to ease the overly restrictive actions which are crippling the interest-sensitive housing market.

I am also concerned with actions that should be taken to raise income limits for FmHA mortgages. This is so that more applicants can pay a higher interest rate, rather than all applicants receiving maximum subsidized mortgages. The income limits for FmHA loans have not been changed since 1977. Therefore, they do not reflect the 13¼% interest rate.

Sincerely,

Glenn Fitzloff

GF: pal

ERA® FITZLOFF REALTY
15 E. 7th St
Litchfield, Minnesota 55355
612-693-3678

Each office independently owned and operated.

Jim

Luverne
FARM STORE and GAS CO.

PHONE 507 283-8666 or 283-2512
South on Highway 75
LUVERNE, MINNESOTA 56156

10-1-81

Vin Weber
514 Cannon Bldg.
Washington, D.C.
20515

Dear Congressman Weber,

I appreciate your concern over interest rates and how they affect the small businessman. I feel that interest rates are the biggest threat facing the small businessman today. Having to pay 19% - 21% interest will force us to change the way we have been doing business for over 30 years.

We are a family owned supplier of farm products such as feed, fertilizer, seed, L.P. Gas and grain storage and drying facilities. We have money borrowed to purchase inventory virtually every day of the year. The old adage about not being able to sell out of an empty warehouse is still true, and we must maintain an adequate inventory to satisfy our farming customer's needs. We have been trying to adapt to the changing times, and our inventories

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are as low as they ever have been throughout the entire year. Our customers expect and require credit. It would be virtually impossible to conduct business on a cash basis. On Oct. 1st the allowable consumer interest charge we are able to legally charge on past due accounts went to 18% yearly. We are presently borrowing money at 19% from our local bank. That means that each and every day a customer owes us money, our profit margin is decreased. In order to survive we have to build this into our prices and the result is an inflated price. The vicious cycle is perpetuated once again.

Not all this credit tightening has been bad. We have had to re-evaluate our credit policies, and have become better money managers. The problem is that we now have to spend such a large percentage of our day harassing old accounts (which does nothing to build customer relations) and regulating finances, that we have no time left to *sell* something. That is what a small business man does best. We are basically a very friendly, outgoing, generous and motivated group of people. We enjoy the challenge of filling the needs of our customers on a personal level. We have now been forced to become bankers, accountants and lawyers. That's not what we enjoy, and that's not what we are good at. We feel that if inflation and interest can be brought under control so that they do not consume our every waking hour, we really *can* stimulate growth in our economy. We need your help.

Sincerely,
Gary Golka

HENRY REALTY

FARMS – HOMES – COMMERCIAL

RUSS HENRY
DENNIS FREDERICKSON

NORTH HIGHWAY 60 AND 71
BOX 334 – WINDOM, MN 56101
PHONE 507-831-2355

October 6, 1981

Congressman Vin Weber
514 Cannon HOB
Washington, D.C. 20515

Dear Congressman Weber:

I would like to bring to your attention a matter that concerns myself along with millions of Americans. I have a serious concern about the extremely high interest rates that have strangled our economy.

As a professional real estate salesman and a member of the National Association of Realtors, I feel that interest rates have been too high for too long! There are many people in this country that would like to purchase homes, but can not because of interest rates in excess of 17%.

Enclosed you will find two articles that I have read in REALTOR NEWS, October 5, 1981 issue. As I read them, I realized that you should read them too. Mr. Weber, not only are real estate agencies and banks hurting from sky high interest, but so are home sellers, buyers, and builders. Sales of new homes in August have plunged 14%. What can you do to help?

Sincerely,

Eric J. Frederickson

Eric J. Frederickson
629 Olson Avenue
Windom, Minnesota 56101

ic
Enclosures

Sales of new homes plunge 14%

WASHINGTON — The housing markets are taking an unbelievable beating, as evidenced by the 14 percent plunge in August new-home sales from July and the 7.1 percent drop in average home prices, said Dr. Jack Carlson, NAR chief economist and executive vice president. The sales figures also reveal a 41 percent drop in new-home sales since August of 1980.

Carlson pointed out that for the one-third of the American public who do not own a home, the prospect for achieving home ownership remains dim so long as interest rates remain high

LOUIS DE CATHELINEAU
612/235-2149

EAGLE REALTY
417 W. LITCHFIELD AVE.
P.O. BOX 1123
WILLMAR, MN 56201
612/235-1572

RICHARD O. ARNE
612/235-4150

October 08, 1981

THE HONORABLE DAVID DURENBERGER
353 Russell Office Building
Washington, D.C. 20510

Re: Interest Rates

Dear Senator Durenberger,

A healthy economy creates a positive national spirit. We need both to survive this decade. Therefore we urge you to;

1.) Hold the budget deficit to under $42.5 billion in fiscal 1982 and balance the budget in fiscal 1984.
2.) Propose to the Federal Reserve Board to allow the money supply to increase at the upper end of its monetary targets to accommodate economic growth and national stability.
3.) Appoint a small business person from an interest-sensitive industry to fill the next vacancy on the Federal Reserve Board, which we understand is expected in January.

You can talk about clean air, Social Security, AWACS, Government Competition, Regulatory reform and abortion, but no issue deserves and demands action like the current depressing interest rates.

Your attention to this matter is earnestly urged.

Yours very truly,

EAGLE REALTY

Richard O. Arne & Louis de Cathelineau
Broker

ROA/jkj

HARDWARE HANK
Norm & Rose Marie Anderson
Jackson, Minnesota 56143 — Phone: (507) 847-2990

October 12, 1981

Honorable Vin Weber
Member of Congress

Dear Vin

I have just received your letter of October 7, 1981 relative to the hearing on the subject of Federal Monetary Policy and its impact on Small Business, Yes, I'll gladly send a statement.

We are a new retail hardware business in a small town. Our annual sales do not yet reach $400,000. We began in 1977 with the aid of an SBA guaranteed loan. We had a good start, with 1979 sales 150% of 1978. (Open only one month in 1977.) Last year, 1980, already showed the effects of tight money, with sales at only 111% of 1979. As a new store, we should still be growing at a greater rate. As of August 31, 1981, our sales are at 93% of sales for the same period of 1980. The general effect of tight money is to hurt sales.

The most direct influence upon us, however, (of the tight money/high interest squeeze) is in our cost of doing business. Rather than allowing a small profit to be used to pay taxes, decrease debt, etc., the cost of money we face is forcing increased debt and eliminating profit and equity. Our interest cost us 5.39% of sales in 1978, 4.62% of sales in 1979, 5.52% of sales in 1980, and as of August 31, 1981, 11.62% of sales. Our total borrowing on long and short term loans has increased from opening day by 53%. At present short term demand notes represent 62% of our borrowing, and that, of course, is at current market interest rates. We now owe as much on short term as our original long term loan included. You must agree this is negative progress.

We, alone, are not a large important business. We do, however, employ 6 people, provide a service to our community, and pay our own way. We're not looking for handouts, but we cannot stay in business under these conditions.

Good sense would have put us out of business long ago, except for two important factors. First, there's no way to sell a business like ours with the current cost of money. As the money market stands there is no incentive to invest in a business that requires risk, work, and much time. Second, we possess a strong faith that this situation cannot and will not be allowed to continue. Our country can't afford to stifle the businesses that offer the only sensible solution to the needs of rural America. Small businesses are the backbone of the rural areas. We can't afford rampant welfare -- we're better off with healthy small businesses.

We are willing to continue to pour effort into our enterprise, if there is hope of recovery. The needs of small business (most of which cannot now choose not to borrow) are such that unreasonably high interest costs compounded with the decreased sales they generate are certain death. Please don't allow this to continue. Thanks in advance for your help.

North Central Agricultural Service, Inc.

Telephone:
(612) 523-1951

Specialists in Farm - Ranch Properties
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P.O. Box 26
822 East Lincoln
Olivia, MN 56277-0026

October 13, 1981

Congressman Vin Weber
514 Cannon Office Building
Washington, D.C. 20515

Dear Vin:

Relative to your letter of October 7, 1981, soliciting comments about the affect on my business of Federal Reserve policy and high interest rates:

1. Those policies have drastically lowered my income, driven down grain prices, driving up costs and making real estate sales very difficult. The past 90 days have been an economic disaster for us.

2. However, in spite of the hardships, I am not complaining about Federal Reserve policy. Instead let's support President Reagan in getting the deficit down immediately! I'd be willing to sacrifice longer in order to correct that underlying problem. Once the deficit is under control, interest rates will come back down.

If necessary, let's even consider the following to eliminate the deficit:

1. Scrutinize government waste and fraud much closer. There are still many problems in that area, including defense spending.

2. Defer some of the tax cuts for enough time to lower that deficit!

It's time to bite the bullet! The job is half done, let's finish it!

Sincerely yours,

Roger Heller
A.F.L.B., A.F.M.

RH/lkj

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BUERMAN HOMES
West Highway 23, Cold Spring, Minnesota 56320
(612) 685-3633

October 13, 1981

Congressman Vin Weber
514 Cannon Building
Washington, D.C. 20515

Dear Congressman Weber:

Enclosed you will find a brief statement on what the high interest rate has done to my livelihood and company.

Thanks for the opportunity to express my thoughts. Sorry for not responding upon your first request.

Sincerely yours,

Clarence Buerman

CB/sb

Vin
I believe in Reagan policies
but interest rates have to change soon
Clare

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BUERMAN HOMES
West Highway 23, Cold Spring, Minnesota 56320
(612) 685-3633

October 13, 1981

EFFECT OF HIGH INTEREST RATE AND THE FED'S MONETARY POLICY

My name is Clarence Buerman, married to Renee Buerman. We have five children.

I am president of Buerman Homes Inc. Renee is secretary-treasurer.

Likewise, I am president of Buerman Realty Inc. and Renee is secretary-treasurer.

Buerman Homes is in the business of manufacturing a pre-cut panalized package. Our market is in a five state area, namely Minnesota, North Dakota, South Dakota, Iowa and Wisconsin.

Prior to October 1979 the Buerman Companies were doing $5 million in volume and had 50 people employed. At peak employment we had 80 employees.

Since Oct. 6, 1979 when the Feds Monetary Policy and the prime started to climb, real estate loans were out of reach for most home buyers and our business started to go to pot.

In 1980 our volume dropped to $2.5 million with 25 employees. Our new single family sales in our real estate company dropped to 10 sales and in 1981 our Real Estate Sales were 2 Single Family Sales with one employee that being myself.

In 1981 our pre-cut panalizing plant is down to three people on our payroll which are all people in management.

In the past two years we were forced to relieve 15 key people, and the balance being skilled trades people.

At this point, due to high interest and the Fed Monetary Policy, Renee and I don't know from day to day whether the business we have worked for in the last 20 years will have the door open the following day.

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Molenaar, Inc.
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Willmar, Minnesota 56201, Box 777
Area (612) 235-5000
WATS 800-328-8944

October 13, 1981

Representative Vin Weber
Congress of the United States
House of Representatives
Washington, D.C. 20515

Dear Mr. Weber:

Allan received a letter from you that he gave me to answer inasmuch as my duties are more in the financial end of our plant. Regarding the high interest rates and its affect on our business, let me state that while in our particular case, we have had money to loan so the high interest has in that way worked in our favor. However, as far as the country itself is concerned, the high interest rates are a major tragedy. The purpose seems to be to discourage consumption and therefore decrease inflation. The result, however, is exactly the opposite since most businesses have to borrow money which adds to their costs which must of necessity be passed on to the consumer. It therefore directly adversely affects inflation. Furthermore, it makes it difficult for business to grow and thus decreases productivity. Again, this adversely affects inflation.

The only realistic way to handle the existing demand and reduce inflation is to control the availability of easy credit. This could be done in a number of ways, one of which would be to require a larger down payment on any time pay sale, and another would be to reduce interest rates for small loans to the point where they would be less attractive than loans to businesses who would then be in a much better position to increase productivity. Both solutions are comparatively simple and would have the effect of creating a saving philosophy such as exists in Japan or at least up until recently existed in West Germany.

I wish to thank you for listening to me and hope that my thoughts may be of some value to you.

Sincerely,

MOLENAAR INC.

Lester V. Molenaar

Lester V. Molenaar,
President

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Fenton
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1005 North Sibley Ave. • Telephone 693-3224
LITCHFIELD, MINNESOTA 55355

October 13, 1981

The Honorable Vin Weber
House of Representatives
514 Canon Building
Washington, D.C. 20515

The Honorable Mr. Weber:

In response to your letter of October 7th, 1981 regarding high interest rates. A statement for the record--"High interest rates are crippling the Auto Industry". We have been saddled with these rates for over two years and have dipped into reserves to stay alive. I believe most dealers are unprofitable for this period. I just had word today that a fine Ford Dealer in Willmar will close the doors on October 15th, 1981. A direct result of interest rates. It is imperative that something is done immediately.

Sincerely,

Richard D. Fenton

Richard D. Fenton, Pres.

RDF:jbw

"Guardians of your driving pleasure since 1939"

OCT 13, 1981

LOREN FEMRITE
FEMRITE ENTERPRISES
FEMRITE CABINETS
RT 2 BOX 20
DAWSON, MINN.
56232

DEAR MR WEBER

AS A RESPONSE TO THE ISSUE OF INTEREST RATES AND THE THE FEDERAL MONETARY POLICY. THIS DISTRICT IS AFFECTING OUR BUSINESS IN TWO WAYS. THE INTEREST RATES AFFECTING FARMING WITH ITS DIRECT AFFECT ON AGRICULTURE RELATED INDUSTRIES AND THE INTEREST RATES FOR HOME~~OWNER~~ MORTGAGES. THESE ARE TWO SEPARATE BUT DIRECTLY RELATED AREAS. FARMERS AND NON FARMING PERSONS ARE NOT INSTIGATING BUILDING PROJECTS BECAUSE INTEREST RATES CANNOT BE MET. MANY INDIVIDUALS HAVE COLATERAL BUT CANNOT SERVICE THE LOAN OR WILL NOT PAY THE INTEREST.

THE INTEREST RATE IS LIKE A DAM IN A STREAM CAUSEING A STAGNENT BACKWATER. THAT STAGNENT BACKWATER IS OUR WORKFORCE AND WHEN WE DO NEED IT, IT WILL UNABLE TO PRODUCE LIKE IT SHOULD AND IF WE FALL SHORT IN PRODUCTIVITY WE WILL BE IN TROUBLE.

Loren Femrite

Southwest Enterprises, Inc.

NORM "SHEP" SCHOEPHOERSTER
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DON MONSEN
(507) 532-9782

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Custom Systems

203 WEST MAIN
MARSHALL, MINNESOTA 56258
507-532-9782

October 13, 1981

The Honorable Vin Weber
Congressman 6th Minnesota District
514 Cannon Building
Washington, DC 20515

Dear Congressman Weber:

I am sorry that I did not respond to your letter of September 14, 1981. We received your letter the day before the hearing date of September 22. I assumed it was to late to write. It seems your letter got lost because stamped on the envelope was, "received unsealed at Minneapolis, Minnesota". I am responding to your letter of October 7, 1981 which we received this morning.

Southwest Enterprises is a small corporation that manufacturers and distributes wireless alarm systems in the agricultural field. We have been in the wireless alarm business about four and one half years. We were very optimistic about business because our sales nearly doubled in 1979. Then in 1980 the economy changed and our sales slowed considerably.

The slow down of our business was mainly caused by high interest.

1. High interest stopped us from borrowing money to expand our markets which are world wide.
2. High interest made us very cautious in a relatively new kind of business. No hiring of new personnel.
3. High Interest made our customers very conservative in purchasing our products. Sales are down.
4. High Interest has given almost everyone a negative attitude about business.

We are still optimistic about our future in the alarm industry. Available money at realistic interest rates would help tremendously.

Thank you for letting us write on the subject.

Sincerely,

Norm Schoephoerster

Norm Schoephoerster
President

NS:ld

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10-13-81

Congressman Vin Weber,
House of Representatives,
Washington, D. C. 20515

Dear Congressman Weber:

In regard to your letter of October 7th, I would like to say that high interest rates have not only hurt my business, but many businesses.

First of all, car dealers have been hurt considerably and of course this means they do not make sales, so they do not advertise as much. The high interest rates have hurt sales of homes and businesses and so the real estate people have been losing money, and they cut way back on their advertising. Then you can add to this all the construction workers that are out of jobs, because of no building, hurting all business places in town, so they cut back on advertising. These are just a few of the places my business has been hurt by the high interest rates.

I don't think there is a business in this entire community that has not felt the "pinch" since the interest rates went out of control. The only ones that really benefit are those with lots of money to put in money market or other high interest savings accounts.

Vin, sometime I would like to talk to you about two other things that I believe need to be done. The first is a balanced budget and the second is putting some teeth in criminal laws, so that people who commit crimes are punished. We will never cut crime unless people know just what penalty they will get for the crime they are involved in. I'll talk to you the next time you are in the area.

Yours truly,

Harold L Norman
Harold L. Norman

KQAD

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DAWSON, MINNESOTA 56232

October 13, 1981

Hon. Vin Weber, MC
Washington, D.C. 20515

Dear Cong. Weber:

I am writing you with reference to the effect of high interest rates and the general high rate of inflation on us as small business men.

Any business needs to expand its facilities at some time or other and these facilities need to be able to support the costs in olved in building and maintaining them. In our case, tthe volume of business mandated some new facilities and we went ahead with aquiring them. Interest rates never used to be too much of a factor in the considerations; but now it is the major one. Expanding gets to be a risky venture in the face of the obstacles.

I guess I cannot understand the Federal Reserve's stand on continuing high interest as a way to cut inflation. All it does in my view is stifle business, cause business failures, unemployment as s result of these failures and other general slowdowns. Whatever happened to the goal of raising the GNP? I have never been one to blame the so-called "money men", but it looks like they want the high interest for those who have it to invest.

Thanks for taking the time to read about our woes.

Sincerely,

Harland E. Thoen
Dawson, Minnesota 56232

American State Bank of Olivia

ASB

BOX 10 PHONE: 612-523-1111 OLIVIA, MINNESOTA 56277

October 13, 1981

Congressman Vin Weber
514 Cannon Building
Washington, D.C. 20515

Dear Congressman Weber:

I received your letter regarding the hearings on Monetary Policy.

I was disturbed to see your emphasis on Fed policy and high interest rates as though these are the cause of the economic troubles we're having. Clearly, they are the symptoms and not the disease.

Total Federal credit demands, including refundings, now exceeds 20% of the total capital raised in this country. That's the root cause of our problems, and if the budget deficit is allowed to grow to 70 to 100 billion this year, I believe that prime could go to 30% and beyond.

I, therefore, respectfully suggest that your time could be better spent working on ways to hold the budget deficit to 42 billion than working with the pressure groups whose purpose is to defeat the program we voted for last November.

Sincerely,

David Fleming
President

DF/bjn

Suburban Commercial Fixtures
5129 Industrial St. / Maple Plain, MN 55359 / (612) 479-2523

October 13, 1981

Congressman Vin Weber
514 Cannon Building
Washington, D.C. 20515

Subject: Interest Rates

Dear Mr. Weber,

I would like to be put on record in stating that current interest rates have affected businesses very gravely and this must be changed very quickly.

Suburban Cabinet and Fixture Co. has been in business since 1950. It is a family business that has struggled for its existance since it began. We do not expect an easy existence or "Easy Street" but do believe that if you are in business you should make more than a wage.

Profit is specifically what makes our country great! However, many people in government and in the private sector have the mentality that someone else who has done a good job should pay for their generous feelings! We (as a country) can not go on this path any further! A balanced budget is a must.

This leads me to interest rates. What you are currently seeing in high interest rates is caused by spending more than you have coming in. Our government has been a terrible example to the individual and to business. Thus, during the 70's with the "get all you can" attitude, many individuals went into personal debt because they knew (Government and Economists told them) it would be easy to pay it off in the future with cheaper dollars! Everyone then started to borrow and since you are taxed on interest profit, why save? Invest it in something that you borrow even more dollars for. Now we have an inflation that only the very rich can afford. The few people that still had money saved, lost it to inflation.

On the business side, many owners did buy new equipment to meet this demand, but again did not have profit or reserves to pay for the equipment and this placed additional pressure on the meager savings available in this country. Most of this highly leveraged business is already out of business. The next effect has already taken place in businesses which were financially sound. We had a good equity position but limited reserves because of the competitive market and lack of profits. Now good sound businesses like ours must borrow to provide cash until the economy turns around. This last situation is the most dangerous for our entire country! When solid businesses are borrowing, it keeps the interest high and unless government balances the budget and lets the people who are not productive and not willing to help start to suffer, this country will soon be in a deep depression.

The company with 30 years experience in designing quality products

Suburban Cabinet and Fixture does commercial work, not residential. We manufacture products for banks, retail stores, grocery stores and restaurants. We deal locally, statewide and nationally. We deal with chains in these groups as well as individuals. The story is the same for all geographic areas of the United States.

Three things must happen immediately:

1. All spending must be below the money that is taken in.

2. People on welfare must no longer be trapped by being supported by all our governments. (Local, State and Federal)

3. The interest rate through the above measures must come down.
To just lower the interest rate would be a cruel joke!

One recommendation I would like to suggest is that people and businesses be taxed differently. Simply stated: If a business sells or manages $1,500,000.00, they would pay 1% tax or $15,000.00. If a person receives $30,000.00, they would pay 10% or $3,000.00. The percentages are only an example, the point is that you cannot deduct for anything! This would cut a tremendous amount of paper work and IRS staff. Most importantly, the rate is the same for all business and individuals so that every one would pay an equal share of the burden and government would help people to earn more instead of being punitive.

Sincerely,

Bruce E. Hagberg

Bruce E. Hagberg

BEH:diw

To Congressman Vin Weber
514 Cannon Bldg.
Washington DC 20515

SWENSON ELECTRIC-+[illegible]
WIRING - PLUMBING - HEATING
321 6TH AVENUE
MADISON, MINNESOTA 56256
598-7515

DATE 10/14/81 SUBJECT

Dear Sir,

High interest rates have knocked sales down to practically zero. And are service Work is slowed way up. We are loosing money rapidly due to above + high cost of everything.

Sincerely
Sidney L. Swenson

Barge's B & B Store

WOOD LAKE, MINNESOTA, 56297
PHONE: 507-485-3470

October 14, 1981

Congressman Vin Weber
House Of Representatives
Washington, D.C.

Dear Sir:

In response to your inquiry as to the effect of the Federal Government's monetary policy I should like to state the following:

First, we in rural southwestern Minnesota find ourselves in an enviroment of declining population, of fewer farmers farming and living on the land, of smaller families or no family, of fewer people in our churches and schools, of declining main streets - (we are the only store left selling new merchandise in our community of 1200 people).

Second we find ourselves in a situation where we might well expand the merchandise selection we offer in order to serve our community better. There are least 4 area that we might expand into. (Other new stores would be better, but it seems that those who are interested cannot get the money and those who have some money are not interested in creating a new business).

It becomes difficult to expand or start a new business because of high interest rates, because of constant inflation and makes one wonder why one should try. (maybe that's why people with money are not interested in creating new businesses) The matter of this constant inflation is wearing me down. Year after year one must continually plow back a portion of the profit in order to maintain inventory because it constantly costs more to buy back what you just sold. I guess I'd like to be able to take out of our business just once all of the profit it supposedly made and what we pay tax on and still have as much inventory for the new year.

These two problems or cahllenges make one think more than twice about a possible expansion or starting a new business. The incentive is weak.

I'd like to see the Federal Government make money availbale to us at a reasonable rate with which we might serve our communities better, which would create some jobs and which might help slow down our population exodus. I8d like to suggest that govern't use some of the millions it is now using to try to buy the friendship of foreign nations (quite unsuccessfully it appears to me) - to help its own people here at home do a job through private enterprise.

Congressman Weber, your efforts are appreciated. Thanks!

Norman Barge

Food And General Merchandise

Franklin State Bank
1618
Members of F.D.I.C.
Franklin, Minnesota 55333

October 14, 1981

The Honorable Vin Weber
House of Representatives
Washington, D.C. 20515

A brief statement on the Rural Economy Outlook here in our Rural area of Minnesota.

I feel that interest rates has a lot to do with business in small towns and also in all of farming states, because of high rates machinery dealers and auto dealers are feeling the first impact.

When sales are down sales tax collections suffer, the new income tax law is only increasing Gov't borrowing thus keeping interest rates high.

I strongly feel that you realize this and will do all you can to trun this around.

Respectfully submitted,

V.S. Sather, Cashier
Franklin State Bank
Franklin, Minn. 55333

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October 14, 1981

Hon. Vin Weber
House Office Bldg.
Washington, D.C. 20515

Dear Congressman Weber: RE: Federal Monetary Policy

Your October 7 letter arrived via U.S. Snail October 13th.

Problems?? Well we are a small business corporation operating a rural area. If indeed a farmer's dollar circulates 7 or more times how well we know it.

Our 1980 Ready-Mix business was down 14% from 1979. October is usually our "boom" month for sales. In 1980 we sold $761\frac{1}{2}$ from October 1 to October 16; this year, 166 yd. In 1980 we sold $654\frac{1}{4}$ yd. fill gravel; for the like period this year, 81 yard and on and on and on. We furnished concrete for 2 or not over 3 houses this year. Years gone by it was 18 to 30 and each unit would take about 50 yards for footings, floors, driveway and sidewalks.

Impeccable sources advise us that N.W. States Cement of Mason City, our supplier for over a $\frac{1}{4}$ century has shut down one kiln or 25% to 33% of production. In normal years they cannot keep up.

17% to 20% interest? Maybe we should move to Red China. I have read we are lending it to them for 8 3/4%. Maybe that's why we've delivered 1 silo job in 2 or more years.

As a life long Goldwater-Harry Byrd conservative I frankly ask you who can unravel a half century of fiscal insanity??

"A SOLID NAME IN CONCRETE"

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WILLETT'S

Sand & Rock Fill Road Gravel
JACKSON, MINNESOTA 56143 Bulk S-O-F-T Water PHONE 507-847-2790
"Concrete Headquarters Since 1927"

Sincerely,

L.J. Willett Sec.
Willett Gravel Co. Inc.
Box 165A R.F.D. 2
Jackson, MN 56143

P.S. On an unallied topic your vote and those of Erdahl, Dan Daniels, Hagedorn et al on Martin Luther King holiday perplexes me. Does he rate with Christmas and President's Day?

Dodge
Dodge Trucks

DELANO DODGE & CHRYSLER
U. S. Hwy. 12 Phone 479-2595
DELANO, MINNESOTA 55328

Oct. 14, 1981

Vin Weber
514 Cannon Blg.
Washington, D.C. 20515

Thank you for this opportunity. Since 1968 I have benn a Dodge, Chrysler, Plymouth dealer. I have served served as President of the Mpls. Zone, 240 plus dealers, Dodge Advertising Association and also presently secretary for the Dodge Advisory board. This position has kept me in touch with many dealers and keeps me aware of their problems.The problems of the auto dealers are similar. The worst at this time is the Prime. Let me share briefly with the high point of my problem.

At the year end of business in 1978 we carried a new car inventory of 92 units. Our interest cost that year was $168.00 per new car sold. This year, thru Sept., I have maintained an inventory fluctuating between 50 to 75 units and my interest factor is $284.50 per new car sold.

Let me state this differently for impact purpose. In 1978 our total new car interest for the year was $55291.00, or 36.7%of our new car gross profit. For the first nine months of this year we have spent $90721.00 for new car interest, while carrying a smaller inventory, This figures out to 88% of our new car gross profit is spent on interest. Thank God for our used car and service business or we would be out of business.

When we started the present Delano Motor Co in 1968 our total dollar volume was $250,000.00 yearly and we had six employees. Today we employ 14 and our sales for the first three quarters this year are 3 million. This dollar volume, and we are showing a bottom line net profit that wouldn't even meet a one week pay period for our employees.

Another way of stating this is in thirteen years we have increased our sales sixteen fold while increasing our work force 2 1/3.

It is about time the government realizes that the small business man is getting tired of working longer, harder, and smarter, to earn only less and less. We need help now with the areas we cannot control. Prime must come down. True, Paul Volcker is emphatic an d states that the only way to get the interest rate down, and keep it down, is to curb inflation.

But, the question is, WHAT PRICE LOW INFLATION!!

AUTHORIZED DEALER CHRYSLER MOTORS CORPORATION

Dodge
Dodge Trucks

DELANO DODGE & CHRYSLER
U. S. Hwy. 12 Phone 479-2595
DELANO, MINNESOTA 55328

Must we see thousands more of small business fold? Must we see ten of thousands more jobs disappear from the private sector? Hopefully, Mr Volcker can see that too much inflation fighting that continues to pentalized America's business community may lead to de-flation.

If there's no business left, there's no job. No jobs means no money. No money, no spending from the work force, eventually de-flation. Watch the price of a hamburger drop when most of America can't afford it.

It is indeed a sad thing when we allow the money people to invest in money and make 20% doing it. For a stronger America we have to start giving the private business community opportunities to make money and create jobs, rather than allowing the present trend of high returns on money invested in money. It time we again start investing in people.

In closing, I am just one small voice crying out. I am getting tired. Many times I feel defeated. But mostly I am angry. The entire span of business needs your help. I do believe that the most critical segment at the present time is the Auto dealer. Because the cost of our inventory is so high we feel the back-breaking crunch of high interest first.

We need the Prime down now, we need your help now. Many auto dealers will not survive much longer unless the prime comes down and stays down.

Thank you,

J. R. Barbre

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WORTHINGTON, MINNESOTA 56187

MEMBER
TELEPHONE
507-376-4171

October 14, 1981

The Honorable Vin Weber
House of Representatives
Washington, D.C. 20515

Dear Sir:

In response to your letter of October 7, I assume that you are looking for percentage decreases in total business for the 1981 year.

Real Estate business is down 80 percent, Insurance business is down 25 percent, new building starts (both dwelling and commercial) are down 85 percent. This amounts to an almost complete standstill in our business community. We cannot survive with 18 to 20 percent interest.

I hope this is the type of reply that you are looking for.

Yours truly,

Wallace Verdugt
Wallace Verdugt

WV:ct

ELECTROMATICS INC.
540 APOLLO AVE. N.E.
ST. CLOUD, MINN. 56301
PHONE (612) 253-9183

October 14, 1981

Mr. Vin Weber
514 Cannon Building
Washington, D.C. 20515

Dear Mr. Weber:

As a small business operation, we experience occasional cash flow problems, thus find it necessary to take short term loans for operational expenses. In situations like this, the unreasonably high interest rates in combination with the low cash flow virtually wipes out any profits that we may have realized for that period.

We have also been looking for some time at relocating our business to a better retail area and to take on a new retail priduct line. With interest so high, it is impossible to move on these actions.

Our normal business activity is down 20% in each of the past two years, again because our customers face the same problems we do.

We do not want to see continued deficit spending and runaway inflation, but to allow this Federal Reserve Board to control and manipulate the economy is ridiculous.

Sincerely,

Lloyd Prigge
President

LP/rp

PROGRESS IN AUTOMATION

RIDLER & WESTBERG
PUBLIC ACCOUNTANTS

P.O. BOX 362
PHONE 235-3727

WILLMAR, MINN. 56201

October 14, 1981

Vin Weber
6th District Congressman
514 Cannon Building
Washington, D.C. 20515

Dear Mr. Weber:

First I would like to thank your office for the White House Tickets your office mailed to us in August. We were not able to get to your office to say thanks, as we were in Washington only 2 days.

Now regarding the interest rate. The high interest rate is having a profound affect on all businesses, large and small. Specially the small. We are an accounting firm, dealing entirely with small firms within the Willmar, Litchfield, Benson, Belgrade, Olivia area. Today in Willmar, the Ford dealer announced his closing and I am sure he will not be the last. We are seeing people struggling to keep their businesses open while trying to pay an interest rate of 18 to 23 %.

The same business was fortunate to show an 8 to 10% profit when he paid interest of 8%, now with the added interest, it is not possible to even stay open.

It was not hard to see, that government had to do something to control inflation. Some of the people that are not making it now are those that spread themselves too thin, and as a result, were caught in the interest crunch.

The thing that is most upsetting, is that the government allows AT&T an increase in rates because a 13% profit is not sufficient when already their net income is in the millions.

The end result of all of this, will be big businesses getting bigger and the little independent fadding from the picture.

To conclude, I firmly agree with Reagan's plans and the steps that arebeing taken. Our liberal attitudes of the past, in giving to anyone, is the real cause of the problems now. I also believe that corruption is so bad that it is probably to late to make much of any head way.

Thank you for this opportunity to express my view and would like to hear from your office regarding this hearing.

Sincerely,

Paul G. Westberg

REDWOOD FALLS SAVINGS AND LOAN ASSOCIATION
Post Office Box 317
WASHINGTON AT THIRD STREET
REDWOOD FALLS, MINNESOTA
56283-0317
Telephone 507 637-8730

October 14, 1981

Congressman Vin Weber
House of Representatives
Washington, D. C. 20515

Dear Congressman Weber:

Reference your letter of October 7, 1981, concerning Federal Monetary Policy and its impact on Small Business.

High interest rates and the Fed's monetary policy will soon make the Savings and Loan business extinct. We need help before it is too late for our business and all of the housing related businesses. Let's keep home-ownership the background of America and it's capitalistic system. It will soon be tooo late.

Please lower the interest rates.

Thank you.

Sincerely,

REDWOOD FALLS SAVINGS &LOAN

Paul W Pryor

Paul W. Pryor
President

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DIVISION AT 31st TEL 612 251-3282
ST. CLOUD, MINNESOTA 56301
ADDL. FACTORY AT LONG PRAIRIE, MINN. 56347

PRECISION PRODUCTION OF MULTIFOCAL LENS-BLANKS

October 14, 1981

Congressman Vin Weber
514 Cannon Building
Washington, D. C. 20515

Dear Congressman Weber:

This letter is in response to your letter concerning the Federal Monetary Policy and its impact on small business.

Lantz Lenses, Inc. is an established manufacturer of Ophthalmic Lenses since 1936. It is a privately held corporation and employs approximately 200 people. There is genuine concern in our firm about the present economy and its affects on the optical industry.

High interest rates have hurt our business for several reasons. Number one, we are experiencing very tight cash flow situations which is becoming an increasingly big problem with regard to our suppliers of raw materials. Number two, high interest rates have made it virtually impossible to develop long range expansion goals. We are in a necessary position to upgrade our production equipment and build a new modern facility to remain competitive in the market place. This will entail a large capital expenditure which we do not feel comfortable with at the present interest rate levels.

Basically this is how high interest has effected our firm in the past year.

Sincerely,

Clair L Gerads

Clair L. Gerads, Vice President
Lantz Lenses, Inc.

CLG/dd

Oftedahl Drug
205 Sixth Avenue
Madison, Minnesota 56256

Richard Oftedahl
Reg. Pharmacist
Store 598-3864
Home 598-3260

October 15,1981

The Honorable Congressman
Vin Weber
U.S. House of Rep.
Washington, D.C.

Dear Mr. Weber:

The current high rate of interest is going to prevent any real recovery of the economy because the real cause of inflation isn't normal spending by the consumer....The real cause of inflation is the US. governments policy of printing money that it doesn't have.....Now when the country is in trouble the only ones most effected are the small business-men and farmers accross the U.S.A...

If all the middle excutives in this country and including the people in government owned a small business they would change this policy now...
The interest rate should be above the inflation rate but keep their only to drive out people out of work..
If you want to se this country really spirt get the interest rate down as the other troublesome areas are being addressed correctly...

Lets together make the system work....Once interest rates come down the country will produce..If it is allowed to continue it will bankrupt the country.

Thank you for allowing me to comment.. ...

Sincerely, R.C. Oftedahl R PH. RCOftedahl

LINFOR
FLUID POWER

October 15, 1981

Congressman Vin Weber
Congress of the United States
House of Representatives
Washington, D.C. 20515

Dear Congressman Weber:

As goes the prime rate, so goes our business. Prime up. Business down. Linfor Incorporated fabricates hydraulic pressure tube assemblies and tube manifolds. Our two major customers are the farm equipment manufacturers (Steiger Tractor, John Deere, etcetera) and the construction equipment manufacturers (Clark Equipment). Both of these fields, farm and construction, are down because of the prime rate.

In 1979 we employed forty people. Today we employ twenty-four. Down 40% in people, almost as much in sales.

Sincerely,

Wenzel A. Lindfors
President
Linfor Inc.

WAL:ema

15600 32nd Avenue North • Plymouth, Minnesota 55340 • Phone: (612) 559-2911 • Telex: 29-0779

Bisbee Plumbing & Heating

Phone (507) 532-6913

Highway 59 North
MARSHALL, MINNESOTA 56258

Mr. Vin Weber
Congress of the United States
House of Representatives
Washington, D.C. 20515

Dear Vin:

Thank you for your letter of September 14th asking if I would care to comment on the impact of high interest rates.

High interest rates were instituted to curb inflation. Inflation is caused by more demand for products than there is available.

High interest rates kill small businesses and competition. It cannot curb inflation.

The way I see it the only way to curb inflation is let the economy go and take the high inflation, untill business recovers and causes more competition which will drag interest rates down.

Our contracting business is closely tied to the economy and farm prices. Right now we are just trying to hang on until the economy recovers.

I don't mind suffering for a purpose but I see none in this.

Yours Truely,

Joseph Mortier

Joseph Mortier

Palmer Printing, Inc. (612) 252-0033
353 North 37th Avenue • P.O. Box 1575
St. Cloud, MN 56302

October 14, 1981

Congressman Vin Weber
720 West St. Germain
St. Cloud, MN 56301

Dear Sir:

We have immediate needs and plans for new equipment and a new larger industrial building, but we are not doing anything until interest rates fall at least 4-6 points.

Yours truly,

M. G. Palmer

Michael G. Palmer, President
PALMER PRINTING COMPANY, INC.

MGP/mlb

HENDERSCHIEDT TRUCK LINE
1923 Spruce Ave., Box 162 • Worthington, Minn. 56187 • Phone 507-376-6313

October 15, 1981

Representative Vin Weber
514 Cannon Building
Washington, D.C. 20515

Dear Sir:

This letter is in response to your request for inpurt regarding high interest rates and the effects that it has on small businesses.

We are a small trucking business operating four company trucks and six leased vehicles. We haul livestock thruout the 48 states.

Fortunately for us, we were able to update most of our equipment about a year ago. The truck dealers were in a need to dispose of equipment before the new year models came out, and we were able to obtain some lower interest rates by shopping around. The best rate we could find was in the 12% area; but a large portion of the equipment that we purchased was at the 15-16% area. With the rates now at 18% and higher, it would be virtually impossible for us to obtain more equipment or to replace anything at this time.

The rates that we have been able to charge for our hauling have not risen at all in the past year. In fact, some are lower now than a year ago. And yet, the costs for parts, repairs, labor, insurance, permits, licenses, and road and fuel taxes have steadily increased. We are still holding our own, barely. We do have a large number of employees that realize that we can't pay more wages and have had to cut back in some other areas in order to keep the equipment moving, hoping for better times in the future.

Our trucks combined mileage comes to over a million miles a year. Needless to say, our equipment must be kept in top condition and replaced frequently. If interest rates stay at the 18 plus level; or God forbid, climb, it will be impossible for us to replace our equipment when it needs doing.

High interest is one sure way to drive the small family businesses like our own completely out. If that day ever comes, the large corporations will have the country at it's mercy.

Sincerely,

Rodney Henderschiedt
Partner, Henderschiedt Truck Line

Octobrr 13, 1981

Congressman Vin Weber
514 Cannon Building
Washington, D.C. 20515

Dear Congressman Weber:

Just a short line to briefly mention a problem caused by high interest rates.

I own 80 acres of wooded land in Crow Wing County. This land is ideally located between 3 good fishing lakes. It has been my intention to develop this land for re-sale of ½ to individuals for construction of homes. The land is such it would serve as an ideal site for year around recreation and it is my hope to develop a tent and trailer camp site.

Because of high interest rates effecting home construction I dare not invest money to develop this property . Also high interest rates make it impossible to recover costs of developement and operation of a camp site.

The camp site would result in employment of an on-site manager. I realize that this is just one small example of how high interest has prevented private enterprise and potential home buyers from investing. My situation would only create one new job, but, it must be an example of something that is happening thousands of times accross this Nation.

Sincerely,

Jim Pederson

Jim Pederson
Lamberton, Minn 56152
703 S. CHERRY ST.

The Hutchinson Agency

Real Estate & Insurance

607 2ND ST. JACKSON, MINN. 56143

PHONE (507) 847-2160

October 16, 1981

Representative Vin Weber
514 Cannon Building
Washington, DC 20515

Dear Congressman Weber:

Recently I received a letter asking how high interest rates and the Federal money policies have effected my livlihood over the past year. In reference to this, I have enclosed two photo copies of literature that can best describe what high interest is doing to the homeowner today.

Sales are at a six year low in the real estate market. Due to the extreme high interest many people are no longer able to afford a home at their present earning capacity. It is hitting the young people very, very hard in trying to establish homes at this time.

I still am firmly not of the opinion of a full subsidized interest on housing, nor the 'no down payment' practice that has been going on for years. However, the high interest and the current market has drastically effected all sales and in my opinion will continue to effect sales until it is brought under control and lowered to a more realistic level.

Also, in my opinion, it is a reason to stop the liberal giveaway programs that have been sponsored from Washington, D. C. In order to give out money at the ratio that the government has been doing the borrowing from the Federal Government, has interfered with the private market by continuing to keep the interest rates up.

I firmly hope that there is a method of getting this interest rate down to a livable base for the people of this country.

If I can help any further, please let me know.

Very truly yours,

Jack

Jack C. Hutchinson

b

MARKETPLACE

ship. Total housing costs go beyond payments for principal and interest and include real estate taxes, utilities, and hazard insurance.

Again, there is substantial variation in these costs among metropolitan areas as seen in the Table 2. Property taxes are particularly onerous in the cities of the Northeast and North Central states as compared to the Sunbelt states of the South and the West.

By adding these housing costs to the already high P & I payments we get a more complete picture of the financial obstacle facing today's homebuyer. Total monthly housing costs in 1981 are highest in San Francisco at $1,731 followed by Los Angeles, New York, and the Nation's Capital. Pittsburgh and St. Louis ranked at the bottom of the list with total monthly housing costs of $847 and $815, respectively.

The deterioration in housing affordability over the last three years has been devastating. In all 15 cities, total housing costs have increased by over 60 percent since 1978. Indeed, in several cities housing costs have doubled over the last three years.

Those areas where housing costs are up the sharpest are also the cities where housing affordability is deteriorating the greatest. San Francisco ranks as the least affordable area with 66 percent of the average family income required to own the average priced resale property. New York places a close second with 62.2 percent of average family income needed to cover housing costs followed by Los Angeles and Boston. At the other end of the scale, 32.8 percent of the average family income is required to purchase the average priced resale property in St. Louis.

It is clear that the future health of housing markets depends upon reversing the upward trend in the costs of homeownership. Expected declines in mortgage interest rates will help to ease the current crisis in housing affordability and reopen the opportunity of homeownership to a broad spectrum of Americans.

Table 1
MONTHLY PRINCIPAL AND INTEREST PAYMENTS ON THE AVERAGE PRICED EXISTING HOME FINANCED AT PREVAILING RATES

	1978	1979	1980	1981*
San Francisco	$598	$809	$1,174	$1,403
Los Angeles	581	757	1,069	1,234
Washington, D.C.	558	646	878	1,048
New York	431	555	811	976
Houston	436	588	790	974
Minneapolis	409	524	711	830
Milwaukee	395	498	721	818
Chicago	433	511	681	812
United States	**382**	**503**	**691**	**810**
Atlanta	364	459	639	767
Baltimore	359	452	593	716
Boston	386	478	637	734
Philadelphia	339	390	560	673
Detroit	342	420	548	625
St. Louis	283	378	516	605
Pittsburg	325	369	512	601

*Estimate
The Metropolitan areas were selected on the basis of availability of data and to provide wide geographic coverage.

Table 2
TOTAL MONTHLY HOUSING COSTS

	1978	1981*	Percent Change
San Francisco	$839	$1731	106.3
Los Angeles	807	1441	78.6
New York	700	1371	95.9
Washington, D.C.	761	1310	72.1
Milwaukee	595	1186	99.3
Houston	568	1166	105.3
Boston	682	1163	70.5
Minneapolis	606	1102	81.9
Chicago	594	1009	69.9
Philadelphia	549	986	79.6
Atlanta	515	968	88.0
Baltimore	543	949	74.8
Detroit	576	934	62.2
Pittsburgh	514	847	64.8
St. Louis	440	815	85.2

*Estimate

Table 3
TOTAL HOUSING COSTS AS A PERCENT OF AVERAGE GROSS FAMILY INCOME

	1978	1981*
San Francisco	41.7	66.0
New York	41.1	62.2
Los Angeles	43.7	55.5
Boston	35.7	46.0
Houston	30.0	44.0
Baltimore	29.1	40.1
Washington, D.C.	31.4	39.6
Atlanta	27.1	39.5
Philadelphia	32.4	39.3
Minneapolis	31.0	39.3
Chicago	29.6	38.4
Milwaukee	29.2	36.5
Detroit	27.4	35.5
Pittsburgh	29.3	34.1
St. Louis	25.8	32.8

*Estimate

REALTOR NEWS

October 5, 1981

Interest rates push home sales to 6-year low

WASHINGTON — Existing-home sales reflecting the depressing effect of record-high mortgage interest rates, which are attributable in large part to the federal government, dropped to their lowest level in six years in August, according to Dr. Jack Carlson, NAR chief economist and executive vice president.

"August home sales were at a seasonally adjusted annual rate of 2,260,000 units," Carlson reported, "off 10.3 percent from the July level of 2,520,000 units and down 43.8 percent from the sales level that was typical before the government policy drove interest rates to record levels starting 18 months ago."

Carlson said the amazing thing is that homes are still being sold in spite of the record interest rates.

Mortgage assumptions

"Our latest survey indicates that sales are occurring through the use of mortgage assumptions and sellers utilizing their equity to help in the financing," Carlson said. "These uses of creative financing typically provide for interest rates in the 12-14 percent range rather than the 17-19 percent rates which seem to be prevalent."

Carlson noted that the August decline occurred after seven consecutive months in which sales appeared to have reached a bottom level and were holding within a narrow 2.49 to 2.66 million sales range.

"The unexpected and further decline in sales can be directly attributed to the record mortgage interest rates, which are taking a terrible toll on housing," he added.

The continuing recession completed its 34th month in August, and during this period the slump has been felt in every region of the nation. Since 1978, he said, resale activity has dropped 35 percent in the Northeast, 44 percent in the South, 44 percent in the North Central region and 49 percent in the West.

"In August, the level of sales held steady in the North Central region, but declines were recorded in every other region, especially the South and West," Carlson said.

The South saw sales decline by a full 120,000 units on a seasonally adjusted basis, 11 percent from last month and 29 percent from last year.

43%

drop

The West experienced a decline of 100,000 units, 20 percent below the month before and 33 percent below 12 months ago.

Despite the low level of home sales, Carlson continued, home prices have not fallen under the strain on the market.

Median home prices

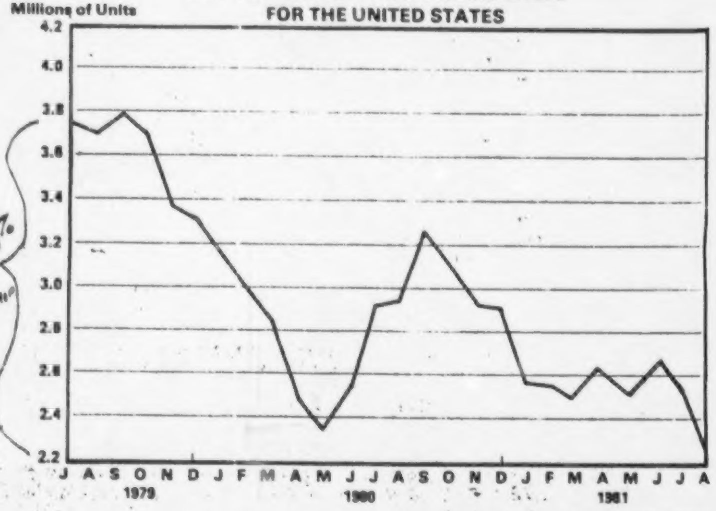
"Last month the median price of an existing home rose 1.5 percent or $900 to $68,400, making up for the $200 price drop in July. Prices increased in every region except the West, where prices dropped by 4.2 percent or $4,200 to $94,700."

In August, the median sales price was only 5.4 percent above the same month in 1980. "However, home prices in 1981 will almost certainly lag 4 percent behind the expected increases in the Consumer Price Index," he said.

After adjusting for lower interest rates associated with creative financing, the drop in real prices of homes may have been 6 to 7 percent since 12 months ago. Although housing price declines are rare, this drop appears modest when considering the huge increase in mortgage interest rates, Carlson added.

"The slow pace of housing construction and sales is creating a shortage that is likely to be reflected in housing prices in the future. Median home prices can be expected to increase by 10 percent during the next 12 months, illustrating the harmful effects of creating a shortage by high interest rates that can only mean greater inflation in the future," he concluded.

EXISTING SINGLE-FAMILY HOME SALES FOR THE UNITED STATES



Source: National Association of Realtors

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Phone 252-6464

UNIFORM RENTAL
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WIPING TOWELS

Dear Vin,

Some 5 years ago I invested my future in small business. At that time, even borrowing huge amounts of money the outlook for a profitable future was very good. However, during the last 2 years the business climate for me has changed very much. My cash flow is very limited because of my original obligation for building and equipment. Selling new accounts now is almost at a standstill because my margin of profit will not support borrowing money for inventory at the present intrest rate. The future does look bleak for my 15 employees and myself if this high intrest rate continues. Please use this letter for any small business concerns.

Thank you,

Norman Gaiduk

Owner

P.S. Thanks for supporting small business.

DISTINCTIVE CAREER CLOTHES RENTAL
Apparelmaster®
LICENSED REPRESENTATIVE

superior
iron inc.

October 16, 1981

Mr. Vin Weber
514 Cannon Building
Washington, D.C. 20515

Dear Mr. Weber:

High interest rates have had more of an impact on my business than any other single factor.

My business is 100% construction related. In previous years, the majority of our business was done in residential construction. The severe decline in home construction due to high mortgage interest rates has necessitated a change in our type of business. As a result, we have had to reduce the number of people we employ. Rather than seeing a continual growth and expansion as I had seen since beginning my business in 1969, I am now feeling that we are standing still and in fact going backward. I feel sure that if interest rates could be brought down we would see a boom in much needed housing construction as well as commercial and industrial construction for investors. This would hopefully make it possible to continue my previous plans for plant expansion and enable me to rehire people presently on layoff and to create more job positions.

It is high interest rates that are keeping me from building a new plant and from purchasing equipment I need as I am diversifying my business. Having to send work out to be done in other shops because of lack of equipment has a significant effect on profits and makes it difficult to remain competitive in a depressed market.

Another effect of high interest rates on my business is an increase in bad debts. I am waiting to be paid on many houses that were sold, but where the sale fell through because an increase in mortgage interest rates before the close of the sale disqualified the buyer for the mortgage. Cash flow is significantly affected as people hold onto their money longer and longer in order to earn high rates of interest or in order to avoid paying high interest on loans.

Thank you for your work on this very important problem facing business today. We are tired of hearing about new offices and departments being set up to tell people how to do basic paperwork in starting a business.

It is high-time we get down to the real problem issues facing business today.

Sincerely,

Donald J. Froland
President

Richard J. Swenson, D.D.S.
Phone (612) 453-2945
Eden Valley, Minnesota 55329

October 17, 1891

Dear Congressman Vin Weber:

In regard to interest rates set by the Federal Reserve Board.

The function of the federal reserve board is to control the rate of money supply and now to control inflation.

Our deficit spending by the Congress and Federal Government has caused a huge federal debt.

I think we have to bite the bullet and keep on high rates until inflation comes down. The high rate of interest has caused farms to stop buying machinery, building and expansion of any projects. The capitol outlay is much less and land values have stabilized. The machinery is becoming worn out and used machinery is going at good prices. The expansion process of one farmer buying another farm has stopped. Land values are stabilized at around $2000.00 per acre, depending on the farm.

The small town merchant has entrenched to remain the same and has not stocked up his inventory. It is a depression attitude.

I am not knowledgeable to be able to solve the problem but I believe in Milton Friedman and Supply Side Economics. We have to get the federal debt down so it doesn't compete with private funds for investment in private enterprise. Interest rates will go up again in six (6) months to finance the huge $60 - $80 billion deficit in the budget.

The best way to keep interest rates down is to balance the budget.

Thank you,
Best Wishes

Richard J. Swenson

Richard J. Swenson

clg

another aspect is commodity prices are down due to high interest charges and so the farmers do not know if they should store or sell.

Don E. Mayer Inc.
762 HIGHWAY #55
HAMEL, MINNESOTA 55340
PHONE: (612) 478-6041

October, 19,1981

Vin Weber
6th District, MN
514 Cannon Bld.
Washington D.C. 20515

Congressman Weber;

Thank you for asking about high interest rates and our business. The interest money we paid out last year compared to the previous year doubled. Our business, instead of expanding, has contracted. We have cut hours, employees, and there have been no pay increases for eighteen months. We once employed fifteen, now we employ ten. Instead of making money, we lost money last year. This is the effect high interest has had on business.

I find it interesting that banking is one of the few industrys expanding in our area. When oil was in short supply, there were investigations and excess profits taxes. When money is in short supply banks go unquestioned. The Federal Reserve is charging high interest rates. Interest rates are justa tax passed on to the American public through the banking industry. Taxes and Federal spending must come down. Even spending on defense.

Sincerely,
Randy
Randall Mayer
Don Mayer Inc.

P.S. Sorry for the typing errors, I even have to type my own letters now!

Mobil

THE
WOODEN SHOE
Inc.

PHONE 612 / 268-3257
RURAL ROUTE 2, BROOTEN, MINNESOTA 56316

October 19, 1981

Vin Weber
6th District, Minn.
514 Cannon Building
Washington, D.C. 20515

Dear Mr. Weber:

In regard to your letter of Oct. 7, concerning interest rates and small business, I have mixed feelings.

On one hand, I don't believe high interest rates have had much real effect on the volume of our business, as it would in the housing industry. But I do question the advisability of staying in business when the after tax return on our business can't compete with the high return of investments such as the Money Market funds. It certainly is easier to invest money in these high returns than to fight government on taxes and paperwork, winding up with a relatively small return for the effort.

On the other hand, I think interest rates must stay high to halt the eroding effect inflation has on everyone, particularly those in the small, rural communities. The only hope I can see to combat both inflation and high interest rates is huge reductions in government spending and the national debt.

Sincerely,

Jan

Jan G. Philipsen
The Wooden Shoe, Inc.

DENNIS A. WATKINS
President

October 20, 1981

Congressman Vin Weber
514 Cannon House Office Building
Washington, D.C. 20515

Dear Vin:

In response to your letter of October 7, I have a few thoughts on the interest rate problem.

There is no doubt that our business has suffered. Although our volume has remained relatively stable considering the economy, profits have suffered because of the cost of borrowing money.

During a meeting with my accountant a couple of weeks ago, I asked him how other clients were weathering the economic storm. His answer was simple and direct. He stated that most of the small businesses were maintaining volume, but that the bottom lines were suffering greatly because of high interest rates. There are simply too many small businesses that cannot pay 20% + for money and write black ink.

It is also obvious what high interest rates have done to the housing industry. The sad part of this story is that not only is the industry suffering, but the general house-buying public is as well. People who are forced to move for career reasons are particularly hard hit. I can tell you personally that this market is bad because I have had a home on the market for over 2 years at a bargain price with no success.

I hope the hearing went well, Vin, and I wish you success in your efforts.

Sincerely yours,

Denny

Denny Watkins

DW/dp

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PEPSI

RICHARD J. BERNICK
President

Bernick's Pepsi-Cola Bottling Company

Sundial Park Box 1184/St. Cloud, Minnesota 56301 612-252-6441
Lakeland Drive Box 455/Willmar, Minnesota 56201 612-235-1370
So. Lake Street Box 55/Duluth, Minnesota 55802 218-727-2400

Schmidt

October 20, 1981

Representative Vin Weber
514 Cannon Office Bldg
Washington, D.C. 20515

Dear Vin:

We have a need to expand our present production and warehouse facilities. Due to the high interest rates we have been forced to cut our expansion in half, thereby eliminating the planned production facilities. This has caused a loss to our community in the form of 7 full time jobs. The high interest rates ate up more profit than the new production facilities would have added.

Sincerely,

RJBernick

Richard J. Bernick

RJB/mh

metal working machine tools

K.E. ERICKSON MACHINERY COMPANY, INC.

7232 Boone Ave. N. Suite 37
Brooklyn Park (Minneapolis) Minn. 55428

(612) 535-0147

October 21, 1981

6th District, Minnesota
514 Cannon Building
Washington, D.C. 20515

Dear Mr. Weber:

I am writing in response to your letter of October 7, 1981.

First of all I would like to give you a little background on our company in order to let you see where we fit into the overall economy. We sell machine tools - the basic equipment used by industry to produce product for consumers and equipment or parts for other industry. Our industry is not a large industry nor is it very will known. However, it is as basic an industry as the steel industry or agriculture. Without machine tools nothing can be produced.

In addition, normally every machine tool sold requires someone to operate it. Thus every one sold means one more job in the market place.

Our company has been in business for 22 years. We are a small family owned business. Although I am not an owner of the business I feel as strongly about the issues involved as if I were. Presently I manage the Minnesota office of Erickson Machinery.

Enough for the introduction. I would like to address the two areas you mentioned in your letter, high interest rates. First there is the real cost and inflationary aspects of the high interest rates then there is an attitude barrier among owners and manages of small business to these added costs of doing business.

It is quiet evident that the current market place will not allow most small businesses to add the extra burden created by high interest on operating capitol into their cost of goods produced. Therefore it must come out of profits or from increased productivity in the case of upgraded equipment purchases. Over 90% of the equipment purchases through our firm is financed in some manner. Availability of adequate financing is very difficult to obtain for most small to medium sized business. To help in this area we have had to add a financing arm to our company. Although this has been advantageous to us it is a further burden on our management.

The other area of concern with high interest rates is that people have a mental block toward high interest. People are not accustomed to thinking this way.

Page Two

Fed's Monetary Policy:

I propose that the real inflation rate of this country will always remain approximately 3 - 4 percent above the Fed's discount rate and that increasing the discount rate will not slow down inflation even though it may tighten the money supply. When the "cost of money" goes up the basic cost of producing the very basic needs of our country goes up proportionately because business depends upon borrowed capitol to do business. This also becomes the cost of Government through cost of goods and services purchased and the cost of maintaining our national debt. No amount of tax policy or government regulations will effect inflation without control of the Fed by businessmen not bankers or financial experts.

Thank you for the opportunity to share my thoughts with you. If I may be of further help please feel free to call on me.

Sincerely,

Ronald G. Wright
Regional Manager

RW/id
C.C. Ken Erickson

Mutual
Service®
Insurance

October 22, 1981

Vin Weber, Representative
6th District, Minnesota
514 Cannon Building
Washington, D.C. 20515

Dear Sir:

The Federal Monetary Policy has affected my livelihood to the extent that clients are taking less coverage with higher deductibles to cut down the expense of carrying insurance. In some cases some are carrying no insurance at all because the high interest rate has caused severe cut backs in all the local small businesses. In fact, a number of small businesses in our area have closed their doors, others are trying to manage with only skeleton crews and sales forces because there is little or no activity in the housing industry, the auto industry, and also the current commodity prices has curtailed the agricultural industry.

All of these decreases in business means fewer jobs, more unemployment, which affects the economy of the whole community.

Respectfully,

Harry Fenstra
pf

Harry Fenstra

HARRY FENSTRA
913 W. Litch Ave / Willmar, Minnesota 56201 / BUS: 235-6466 RES: 235-8717

Mutual Service Life Insurance Company/Mutual Service Casualty Insurance Company/Modern Service Insurance Company

First Bank
Sauk Centre

First National Bank of Sauk Centre
Corner of Sinclair Lewis Avenue and Main Street
P.O. Box 306
Sauk Centre, Minnesota 56378

October 23, 1981

Honorable Vin Weber
6th District Congressman
514 Cannon Building
Washington, D.C. 20515

Dear Mr. Weber:

I appreciate the opportunity that you have given me to respond on how interest rates affect our small businesses here in Sauk Centre. I believe that the high interest rates have had a significant impact on our local economy.

Our farmers interest expense has about doubled in the last year and a half, therefore, putting them in a very tight money situation and eliminating any new purchases that they are able to make in regard to machinery and autos. Our area is pretty much dependent on farmers, and when this happens it has a double effect on our businesses. Their sales are down, plus they still have to finance their inventory with the high interest rates. I don't believe that we had any businesses that I can really point that went broke because of the high interest rates, but we are seeing quite a few of them struggling. We are in hopes that rates will go down, as I am sure everyone else is also.

Sincerely,

Dale J. Emmel

Dale J. Emmel
President

DJE:jk

Member First Bank System

Mr. Gary W. Pestello
832 N 37th Avenue
St. Cloud, MN 56301

October 26, 1981

Congressman Vin Weber
House of Representatives
Washington, DC 20515

Dear Congressman Weber:

Thank you for giving me an extended opportunity to submit a statement on Interest Rates, and I apologize for not writing on this matter earlier.

I believe you and I do agree that some of our current monetary policies is affecting our business and our private lives.

We, in the Graphic Arts, deal in raw materials that constitute 50% of the selling price of a job. Paper companies require their money at the time of shipment, which is prior to printing and billing a customer. As a result, most of a printing company's paper is purchased on borrowed money. I don't think I have to spell out the effect this has on the economy, as all the way down to the consumer the higher interest rates are passed on. This is just one example. Another would be equipment purchases. High interest rates are counterproductive to the 10, 5, 3 depreciation schedule just passed.

As far as affecting my private life, I say just one thing, I will not build a house until things are more reasonable. Many people feel this way, which of course affects many industries.

I support your effort to change the Fed's Monetary Policy, however, the changes should remain within the guidelines of President Reagan's Overall Economic Plan.

Sincerely,

Gary W. Pestello

FROM THE OFFICE OF THE PRESIDENT **BUSINESS INCENTIVES, INC.**

October 28, 1981

Congressman Vin Weber
514 Cannon
House Office Building
Washington, D.C. 20515

Dear Congressman Weber:

The governing of the high interest rate by the Federal Reserve Board is absolutely wiping out small business and is becoming almost frightening. Isn't there something you can do about it?

Please help us,

Guy Schoenecker
President

GS/WJH

7630 EAST BUSH LAKE ROAD
MINNEAPOLIS, MN 55435
TEL: 612-835-4800

Mailing Address: P.O. Box 1610 • MINNEAPOLIS, MINNESOTA 55440 • TELEX 29 0587

DAN MARSH DRUGS, Inc.

517 - 523 Mall Germain P.O. Box 580 St. Cloud, Minn. 56301 Phone (612) 251-1121

October 28, 1981

The Honorable Vin Weber
House of Representatives
514 Cannon Building
Washington, DC 20515

Dear Sir:

Thank you for your letter of September 14, 1981 requesting input from Small Business.(Job Creation and Revitalization of Small Business), and your follow up letter of October 7th. 1981.

I would regard inflation and high interest rates as equal partners as the hindrance of small business. Then comes legislated wages, high SS costs and income taxes, both for the individual and the corporation. Then there is the increases in the Workmans Compensation rates, the Unemployement tax, Real Estate Tax(which harbors the School System tax) and you could go on.

To start regarding high interest rates on January 19 and January 2nd 1976 our corporation borrowed quite a large sum for operating expenses and inventory. The interest rate at that time was only 8 3/4% and new has risen to 19.5% only 60 months later. We have managed to decrease the loan in the earlier perion to about one-half of the original. During the past few years all we have managed to do is pay the interest. Now couple the increase in interest to the increase of inflation of the wholesale prices over the last five to seven years and you can see the problem. We cannot take a full mark-up on the new prices as we must remain competitive. Costs in all areas go up (light, heat,labor,supplies etc) and they seem to have taken the full advantage of the inflation. Costs go up about twice a year from 7 to 10% each time and we end up with a lower gross and net profit. With the increase of wholesale costs and the high interest rates, even on a modest loan, there is just no way to remodel, expand etc. Just to stay in business is a challenge. We intend to survive, but intentions, even though the best often doesn't insure the successful outcome.

I was going to write a separate letter regarding the Central Minnesota Group Health Plan. Please see copy of letter I received which is enclosed. Unless they are generously funded Federally or state I cannot see how they can make it go on the limited hours they plan to stay open and the only five thousand or so dollars of business they do per month. How can they build, supply, fixture, staff and pay the utilities for a pharmacy all out of five thousand dollars per month. This is unfair competition to us.

page two ....The Honorable Vin Weber

While I am at it I am enclosing a letter from the PHP (Physicians Health Plan of Minnesota. We have always tried to cooperate with them and work fairly with them. Both of the above groups made grand promises a couple of years ago when they introduced the plans. Now it seems to be our fault that the planning has not worked out. They have run into inflation and the other problems like we have and they seem to be blaming us. How can they arbitrarily set a fee state wide which I think to be unjust. We have to be realistic and charge a reasonable profit, and this cannot be set by some outsider that has no figures on our overhead, costs of merchandise etc. Three or four years ago we spent around four hundred dollars to pay a CPA to figure out exactly what our cost of filling a prescription was. This was at the request of the Welfare Board. We gave them the figures and they have set up a schedule which I think is quite fair, compared to a fixed one price fee. All schedules have to be adjusted as inflation increases and this is important. We pharmacies cannot talk to each other about this, or agree to do something about this as it would be interpreted as collusion. So where do we go from here?

Also we have a St. Joseph Pharmacy/Clinic in St. Joseph Minnesota which has been in operation for a number of years. It is a HMO type and is subsidized by the tune of a hundred plus thousands of dollars a year. It can't make it on its own because it is not really needed. If it were needed it would certainly be able to survive without this government help.

In general I think this type of government help is wrong in as much as they are pitting them in direct competition with us. Our chances of survival are getting to the point where they are becoming nil. If this is a free enterprise system, it must be a new type which is so modified that it is not recognizable.

I originally started this letter back in September. My wife and I then decided to take a trip to Washington, DC and you were very gracious to arrange for a trip through the White House. When we arrived on the 14th. the young lady in charge of your office had the tickets all ready for Friday the 16th. We enjoyed the trip through the White House and La Donna and I want to thank you very much. We also want to thank you for stopping to greet us on the way out of your office even though you were in a rush to a vote (probably the AWACS problem). It was good seeing you again.

The best of luck to you and thanks for the good job you are doing.

Very truly yours,

George F. Reisdorf

Enclosures: CMGH Letter
PHP Letter